S. Hrg. 99-624

OVERSIGHT HEARINGS ON U.S. TRADE POLICY

HEARINGS

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST SESSION

NOVEMBER 14, 20, 21, 1985

Printed for the use of the Committee on Finance

U.S. GOVERNMENT PRINTING OFFICE
57-470 O
WASHINGTON : 1986

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

S 361-69

COMMITTEE ON FINANCE

BOB PACKWOOD, Oregon, *Chairman*

ROBERT J. DOLE, Kansas
WILLIAM V. ROTH, Jr., Delaware
JOHN C. DANFORTH, Missouri
JOHN H. CHAFEE, Rhode Island
JOHN HEINZ, Pennsylvania
MALCOLM WALLOP, Wyoming
DAVID DURENBERGER, Minnesota
WILLIAM L. ARMSTRONG, Colorado
STEVEN D. SYMMS, Idaho
CHARLES E. GRASSLEY, Iowa

RUSSELL B. LONG, Louisiana
LLOYD BENTSEN, Texas
SPARK M. MATSUNAGA, Hawaii
DANIEL PATRICK MOYNIHAN, New York
MAX BAUCUS, Montana
DAVID L. BOREN, Oklahoma
BILL BRADLEY, New Jersey
GEORGE J. MITCHELL, Maine
DAVID PRYOR, Arkansas

William M. Diefenderfer, *Staff Director*
Michael Stern, *Minority Staff Director*

CONTENTS

ADMINISTRATION WITNESSES

Page
Ambassador Clayton Yeutter, U.S. Trade Representative 9
Stern, Dr. Paula, chairwoman, International Trade Commission 94
Hon. Janet L. Norwood, Commissioner of Labor Statistics, U.S. Dept. of Labor 110

WITNESSES

Aho, Michael, senior fellow for economics, Council on Foreign Relations, New York, NY 363
AFL-CIO and International Union, United Automobile, Aerospace and Agricultural Implement Workers of America, Owen Bieber 148
Agrico Chemical Co., D.W. Calvert 384
American Express Co., Harry L. Freeman 224
Bieber, Owen, vice president, AFL-CIO, and, president, International Union, United Automobile, Aerospace & Agricultural Implement Workers of America 148
Brookings Institution, Robert Z. Lawrence 338
Calvert, D.W., chairman, Agrico Chemical Co 384
Cargill Inc., W. Brendan Harrington 419
Conner, Jim H., chairman, Trade Reform Action Coalition 427
Council on Foreign Relations, Inc 363
Davis, Charles, corporate secretary, Electro Scientific Industries, Inc 274
Eisen, Robert F., Greenwood Mills, Inc., New York, NY 206
Electro Scientific Industries, Inc., Charles Davis 274
Freeman, Harry L., executive vice president, American Express Co 224
Greenwood Mills, Inc., Robert F. Eisen 206
Harrington, W. Brendan, public affairs representative, Cargill, Inc 419
Hufbauer, Gary C., Wallenberg professor of international finance, Georgetown University 326
International Ladies Garment Workers Union, Herman Starobin 192
Jackson, John H., professor of law, University of Michigan 289
Lawrence, Robert Z., senior fellow, the Brookings Institution 338
Leedy, R. Allan, Jr., vice president, secretary and general counsel, Tektronix, Inc 263
Mack, James H., public affairs director, National Machine Tool Builders' Association 212
National Machine Tool Builders' Association, James H. Mack 212
Regula, Hon. Ralph, U.S. Representative, Ohio 259
San Francisco Mercantile Co., Laney Thornton 234
Starobin, Herman, director of research, International Ladies Garment Workers Union 192
Tektronix, Inc., R. Allan Leedy, Jr 263
Thornton, Laney, president and principal, San Francisco Mercantile Co 234
Trade Reform Action Coalition, Jim H. Conner, chairman 427

ADDITIONAL INFORMATION

Press release announcing hearings 1
Prepared statement of:
    Senator Lloyd Bentsen, Texas 1
    Senator Max Baucus, Montana 2
        Letter to Chairman Bob Packwood 4
        Chart on the U.S. share of the Japanese semiconductor market 6

Page

Prepared statement of—Continued
- Ambassador Clayton Yeutter 13
- Answer to question from Senator Pryor 50
- Dr. Paula Stern, Chairwoman, U.S. International Trade Commission 97
- Dr. Janet L. Norwood, Commissioner, Bureau of Labor Statistics 113

Statement of Owen Bieber, president, International Union, United Automobile, Aerospace & Agricultural Implement Workers of America 151
- Herman Starobin, Ph.D., International Ladies' Garment Workers' Union, AFL-CIO 194
- Robert F. Eisen, Greenwood Mills, Inc 208
- James H. Mack for National Machine Tool Builders' Association 214
- Harry L. Freeman 226
- F. Kenneth Iverson, Nucor Corp 236
- R. Allan Leedy, Jr., vice president, secretary, and general counsel, Tektronix, Inc 265
- Charles Davis, corporate secretary, Electro Scientific Industries, Inc 276
- John H. Jackson, Hessel E. Yntema, professor of law, University of Michigan 293
- Gary Clyde Hufbauer, Wallenberg professor of international finance, Georgetown University 329
- Robert Z. Lawrence, senior fellow, the Brookings Institution 340
- C. Michael Aho, senior fellow, Council on Foreign Relations, Inc 366
- D.W. Calvert, chairman of Agrico Chemical Co 402
- W. Brendan Harrington, Cargill, Inc 421
- Jim H. Conner, chairman, Trade Reform Action Coalition 429

COMMUNICATIONS

Statement of Mitchell J. Cooper on behalf of the Footwear Division of the Rubber Manufacturers Association 66

Statement of Harry First, professor of law, New York University 68

Statement of Edson I. Gaylord, president, Ingersoll International 242

Consumers for World Trade 245

Testimony of Ron Kahle, president, National Pork Producers Council 249

Statements:
- American International Automobile Dealers Association 473
- Paul T. Murphy, vice president, National Foreign Trade Council, Inc 506
- Richard M. Brennan, for Coalition for International Trade Equity 523
- Robert L. McNeill, executive vice chairman, Emergency Committee for American Trade 540
- Coalition To Promote America's Trade 546

Statement, Chamber of Commerce of the United States of America 569

U.S. Council for an Open World Economy, Inc., by David J. Steinberg 599

National Retail Merchants Association 603

OVERSIGHT HEARINGS ON U.S. TRADE POLICY

THURSDAY, NOVEMBER 14, 1985

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The committee met, pursuant to notice, at 10:34 a.m., in room SD-215, Dirksen Senate Office Building, the Honorable Bob Packwood (chairman) presiding.

Present: Senators Packwood, Danforth, Chafee, Wallop, Symms, Grassley, Long, Bentsen, Moynihan, Baucus, and Pryor.

[The press release announcing the hearing and the statements of Senators Bentsen and Baucus follow:]

[Press Release No. 85-087, Tuesday, Nov. 5, 1985]

OVERSIGHT HEARINGS ON UNITED STATES TRADE POLICY

The trade policy of the United States will be reviewed by the Committee on Finance in hearings scheduled November 14, 20 and 21, Chairman Bob Packwood (R-Oregon) announced today.

The round of hearings will begin with a 10:30 a.m. session on Thursday, November 14, 1985.

The committee's hearings on Wednesday, November 20, and Thursday, November 21, are scheduled to begin at 9:30 a.m.

All of the trade policy hearings are scheduled for Room SD-215 of the Dirksen Senate Office Building in Washington.

Senator Packwood will preside at all of the hearings.

The Chairman said the three days of hearings would review U.S. policy toward both "fair" and "unfair" trade practices.

Senator Packwood noted that the current debate in the Congress over the appropriate legislative response to the growing U.S. trade deficit often has focused on the "unfair" trade practices of foreign nations.

"I am concerned that the distinction between 'fair' and 'unfair' trade practices often is lost in this debate," Senator Packwood said. "I am concerned that we are not realistically facing up to the challenges of 'fair' trade.

Because of the release by the Reagan Administration of its analysis of foreign barriers to U.S. exports, the Committee on Finance hearings will afford a timely opportunity to examine the distinction between 'fair' and 'unfair' foreign competition and a sensible U.S. trade policy which reflects that distinction," Senator Packwood said.

Witnesses at the trade policy hearings will be asked to address at least one of these questions:

1. How should "fair" and "unfair" trade be distinguished?
2. Can the United States compete with "fair" trade?
3. How should the United States respond to foreign "unfair" trade practices?

STATEMENT BY SENATOR LLOYD BENTSEN

Mr. Chairman, the first National Trade Estimate—delivered to us by the Administration this past October 30—is not everything I had hoped it would be.

It does establish one thing, though: the Administration effort to use Section 301 of our trade law to force down foreign trade barriers is puny by comparison to the job at hand.

In response to pressure from Congress to do something about unfair trade, the President over the last several weeks has dragged out four ancient disputes and launched 301 cases.

It'll be at least a year before those cases are resolved and when they are it will mean, optimistically, an increase in U.S. exports of $300 million to $400 million a year.

By comparison, the National Trade Estimate lists 250 pages of foreign trade barriers. The estimate provides the cost to us in lost exports for only about 15 percent of the barriers. But even for that small percentage the loss amounts to about $4½ billion in exports each year.

Mr. Chairman, the Senate Democratic Working Group on Trade Policy went to Ambassador Yeutter last summer and asked him—under Section 305 of the 1974 Trade Act—for information specific trade barriers in seven foreign markets: West Germany, South Korea, Brazil, Canada, Mexico, Japan and the European Community.

We appreciate the Ambassador's response to us, in a timely fashion, in spite of the large workload he and his staff are currently carrying.

Mr. Chairman, the first National Trade Estimate—delivered to us by the Administration this past October 30—is not everything I had hoped it would be.

It does establish one thing, though: the Administration effort to use Section 301 of our trade law to force down foreign trade barriers is puny by comparison to the job at hand.

In response to pressure from Congress to do something about unfair trade, the President over the last several weeks has dragged out four ancient disputes and launched 301 cases.

It'll be at least a year before those cases are resolved and when they are it will mean, optimistically, an increase in U.S. exports of $300 million to $400 million a year.

By comparison, the National Trade Estimate lists 250 pages of foreign trade barriers. The estimate provides the cost to us in lost exports for only about 15 percent of the barriers. But even for that small percentage the loss amounts to about $4½ billion in exports each year.

Mr. Chairman, the Senate Democratic Working Group on Trade Policy went to Ambassador Yeutter last summer and asked him—under Section 305 of the 1974 Trade Act—for information about specific trade barriers in seven foreign markets: West Germany, South Korea, Brazil, Canada, Mexico, Japan and the European Community.

We appreciate the Ambassador's response to us, in a timely fashion, in spite of the large workload he and his staff are currently carrying.

STATEMENT OF SENATOR MAX BAUCUS

Mr. Chairman, I congratulate you on holding these hearings on unfair trading practices.

The question of unfair trading practices is simple on its face but it grows ever more complex.

I'd like to start with the simple. Many foreign trading practices are not complex. They are very simple, yet devastatingly effective, barrier to U.S. trade.

Let me give you a few examples of these unfair trade practices.

This is a piece of American plywood. American producers are some of the most efficient in the world.

But you won't see much of this plywood in Japan, because they impose a 15 percent tariff on plywood imports. And, despite a personal and public pledge by Prime Minister Nakasone on the MOSS talks—a pledge made 11 months ago—the Japanese refused to budge.

Second, take a look at these American cigarettes. But if you take them into Korea, don't give one to your host because in Korea it is a crime for a Korean to possess an American cigarette.

If a Korean is caught with these cigarettes in Korea, he can be fined up to $1,250 and imprisoned.

In Korea, they say that smoking American cigarettes can be hazardous to your health.

Not all barriers are as blatant as these. Some illustrate the difference between what the Japanese call Hone and Tatamae.

Hone means appearance and Tatamae means reality. The chart tells the story. These bars represent the U.S. share of the Japanese semiconductor market. My colleagues will notice that the bars never grow. In 1974 the Japanese agreed to eliminate their quota. That's appearance. But in place of the quotas they installed a complicated domestic cartel system. That's reality. The difference is huge.

Those are just a few examples of the unfair trading practices the United States confronts.

About a week ago the Reagan administration published this Annual Report on National Trade Estimates.

This report lists 227 separate restrictions on U.S. exports.

That's 227 good reasons why we should be here today.

And that's 227 good reasons why this Administration must act now to eliminate foreign unfair trading practices.

Together these practices reveal a pattern of behavior that is killing us in international trade.

It is a pattern too long ignored. The trade problem is not a political problem to be swept under the rug.

It is an economic problem that we must confront head on.

Unfair trading practices like those I have shown today must be eliminated. Nothing could be more clear.

But if we move from simple through the subtle things get murkier. There are other foreign practices that are not clearly unfair.

These are more complicated—but very important. Let me raise a few.

One of the greatest problems facing American industries today is low foreign wage rates.

Chinese textile workers, for example, are paid only 16 cents an hour.

And the Chinese workers work under low-quality conditions that reduce production costs further.

With wages and conditions like that, it's no wonder that American workers can't compete.

The questions I ask is this: can these labor practices be deemed unfair trading practices?

That's not an easy question to answer.

On one hand, we do not have the right to impose our wage rates and living standards on poorer countries struggling to modernize.

On the other hand, do we not have a right to prevent others from pulling down our living standards?

At what point can we say that low wages and/or inhumane working conditions meet some universal definition of unfairness?

I do not know the answer to these questions.

But I do know that we must begin to ask these questions now, because the issue is going to be with us for a long time.

Yesterday I introduced an amendment to the textile bill that would require the ITC to study this issue and for the Departments of Commerce and Labor to recommend rules and principles that might be incorporated in a universal labor code, if appropriate.

That amendment was approved by the Senate.

However, I expect the textile bill will be vetoed by the president and not become law.

That does not eliminate the need for us to look at this question. I think we need to start thinking about these issues. At the appropriate time, Mr. Chairman, I will ask that the Finance Committee request this study from the ITC under section 332.

This line of questioning can be applied even more broadly. What about differences in health and safety standards? In pollution controls? What is unfair and what is a logical choice for a given country?

We in the United States have coasted along, smug in the belief in our own superiority. If we are to modernize our trade laws, we must deal with the world as we find it rather than as we wish it was. That is a big challenge and it requires a great deal of information. Asking questions is only a beginning—but it is a beginning we must make.

U.S. SENATE,
Washington, DC, July 17, 1985.

Hon. BOB PACKWOOD,
Chairman, U.S. Senate Finance Committee,
Washington, DC.

DEAR MR. CHAIRMAN: As you know, the growing trade deficit is undermining America's fundamental economic strength. Many U.S. companies are losing their footholds in foreign markets and drowning in a flood of imports here at home.

Given this trade crisis, I believe that Congress must enact a tax reform package that improves, not impedes, America's international competitiveness. During the Finance Committee's tax reform hearings, many of us have made this point by raising concerns about the impact enactment of the President's tax reform proposal would have on our competitiveness.

Determining this impact is, or course, a very complex issue. Tomorrow's hearing will shed more light on the issue. But I believe that further and more detailed information is needed before we begin drafting our reform bill.

More specifically, an International Trade Commission study would make a valuable contribution to our deliberations. Therefore, I believe that the Finance Committee should request an ITC study, pursuant to section 332 of the Trade Act, of the impact enactment of the President's tax reform proposal would have on America's international competitiveness. I respectfully urge that you support such a section 332 request and arrange to submit a formal Committee request as soon as possible.

Sincerely,

MAX BAUCUS.

The CHAIRMAN. The committee will come to order, please. I think maybe a point of order is being raised on the floor, so, rather than delay this hearing any longer, I think we will start and hope to get a fair distance along. This is the first of three trade hearings scheduled in the immediate future. Then, when Senator Danforth puts his bill in, we will have other hearings that he has requested to be scheduled on his bill; but it seems to me that we are finally coming to a place where there are three principal, major issues to which we need to address ourselves. One is under section 201 of the International Trade Commission: Is the President bound to respond in the way that the International Trade Commission suggests, or is he going to be left with some option to look at the entire issue from a national standpoint. Or, if put more bluntly, if the International Trade Commission finds that shoes are injured and they suggest some kind of relief, does the President have to accept that, even if that may hurt agriculture and chemicals or other exports? Or can he weigh the country's interests? Two, in terms of section 301, and unfair trade practices, are we going to decide for ourselves henceforth, unilaterally, what an unfair trade practice is and announce it to the world, whether or not the rest of the civilized world accepts that as an unfair trade practice or not. Three, are we henceforth going to say that wage differentials, especially quite disparate wage differentials, between the United States and some other country, are ipso facto an unfair trade practice? Or if we don't call it that, are we going to say that wage differentials are so great that in certain areas we simply cannot compete, and we will not just give those industries 2 or 3 or 5 years time to adjust? We will give them permanent protection because they cannot compete. In my experience in dealing with some of those industries, they have not quite been willing to say: Our problem is that we cannot compete against the wage differential, now or forever. They will cloak it in the multifiber agreement, or they will cloak it in some kind of dumping or countervaling duty issue or some kind of unfair practice; but a few of them, to their credit, have been willing to say: Our problem is that we can no longer pay our workers $7 an hour when workers competing with us with exactly the same kind of machines are making 50 cents an hour. And that is a fair argument; and that is an issue that ought to be addressed, and it ought to be addressed on that basis because, if the United States is going to make a decision that all industries with disparate wage levels are going to get permanent or quasipermanent protection, then we are not talking about just one or two industries. We are probably talking about three-quarters of the industries in the United States, and we are talking about an entire change of philosophy from what has been our trade position since at least Cordell Hull or the end of World War II. So, this will be the first of the hearings. I hope the witnesses will be able to address themselves to those issues. Senator Baucus?

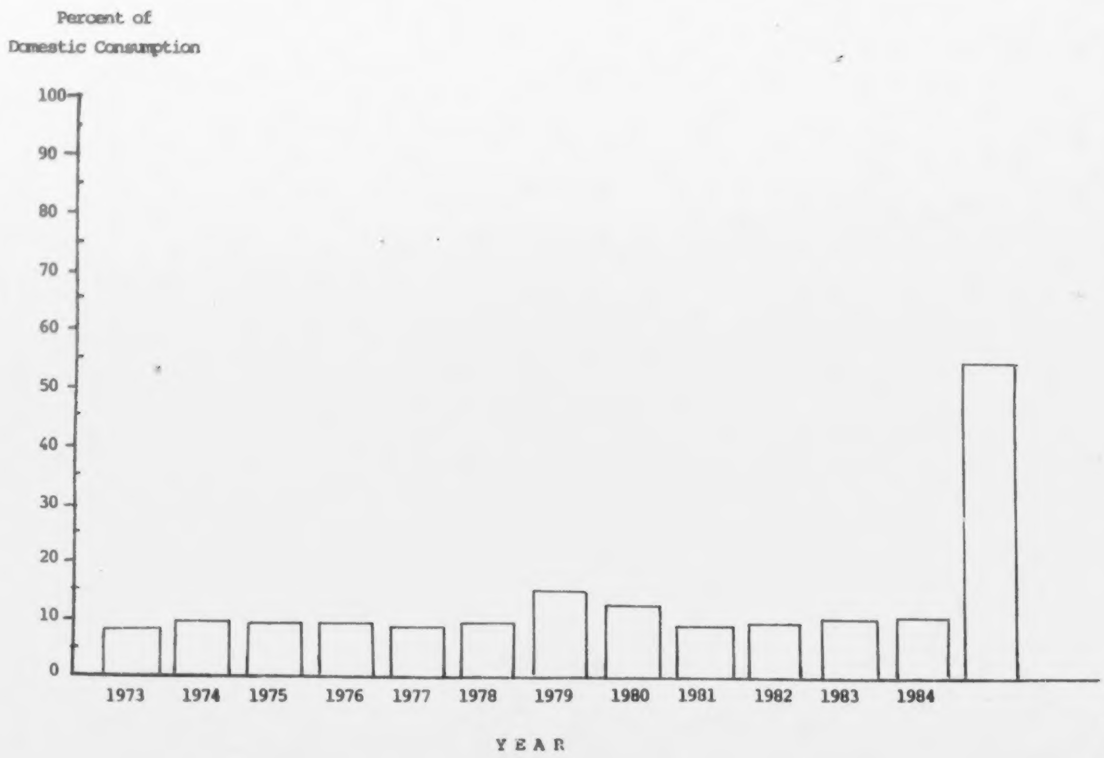
Senator **Baucus**. Thank you, Mr. Chairman. Mr. Chairman, I want to thank you very much for holding this hearing. It is necessary, obviously, to more firmly address what constitutes an unfair trading practice; and I think the questions you have asked go a long way toward establishing that. As we begin, though, to try to determine what constitutes an unfair trading practice, I would like to make a few observations; namely, there are various levels of complexity of unfair trading practices that other countries practice. To some degree, I think the United States is not Simon Pure—we are not as clean as the driven snow, certainly not immediately following a snowstorm. [Laughter.]

But it seems to me that the practices of other countries are also in many respects unfair and have to be addressed. However, there are various levels of complexity of unfair trading practices. For example, some are very clear; they are very simple. I have in my hand here a piece of particle board. This particle board has a 12-percent tariff as it enters Japan. When particle board enters the United States, it has a 4-percent tariff. So, the tariff in Japan is three times as much for particle board entering Japan as it is for particle board coming into our country. That is very simple and very direct. Another example of something that is simple and direct is the practice and the law in Korea with respect to cigarettes. In Korea, it is a crime for a Korean national to smoke or possess American or foreign cigarettes. There is a fine up to $1,250 and also with a punishment of imprisonment. The disparity there is very simple. It is not a crime in America for Americans to smoke foreign cigarettes, but in Korea it is a crime. It seems to me that is very simple and direct. That is an unfair trading practice that the country of Korea undertakes and it has to be changed. Third, though, there are unfair trading practices in other countries that get a little more complex, but they are just as devastating.

[Showing of chart.]

U.S. SHARE OF THE

JAPANESE SEMICONDUCTOR MARKET



Senator Baucus. There is a chart over here that some of you can see; and unfortunately some of you cannot see it. I think it demonstrates a more complex trading practice but devastating nevertheless. Essentially, it shows the level of market penetration of the United States ability to sell semiconductors in the country of Japan, beginning back in the year 1972. Approximately 10 percent of the semiconductors purchased in Japan are American semiconductors—10 percent. The chart shows that it has been about 10 percent every year, up to and including this year. Until 1975, there was a quota on American semiconductors into Japan. In 1975, Japan eliminated the quota; so you would expect that the United States could sell more semiconductors in Japan after the year 1975, but that is not what happened. The chart shows that it was still 10 percent, from 1975 up to the present. Why? Because Japan entered into a cartel arrangement among its major purchasers in Japan, that is the major firms in Japan—the electronics firms—began to buy among themselves. It was a cartel arrangement, so the United States did not sell American products in the country of Japan. Compare that with American market penetration worldwide. The chart shows, the blue line, that it is 50 percent. So, whereas the American penetration worldwide, but for Japan, is 50 percent, the American penetration of the semiconductor industry in Japan is still 10 percent. Obviously, this is an unfair trading practice.

Mr. Chairman, I suggest that this is just one of many examples of the kinds of practices that we have to address today, and I am glad Ambassador Yeutter is here. I want to compliment the Ambassador, too, because I know he is working on the list of 227 unfair trading practices that the administration published and listed. To me, that is 227 good reasons for holding this hearing today, so we can identify those and concentrate on them. It is clear that that is not the only problem that faces America's competitive position, nor the only reason that it is hard for us to trade as well as we might. Nevertheless, it is also clear to me that there are very definite, fundamental unfair trading practices that other countries do engage in. So, we should not keep our eye off that mark, particularly as we move toward a new GATT round. We are going to have a new GATT round. There are going to be new GATT talks. As we give new GATT authority, it seems to me that we have to be very clear and very definite in the kind of authority we give and to make sure that that new GATT round does focus on these kinds of practices. Thank you, Mr. Chairman.

The Chairman. Senator Wallop.

Senator Wallop. Thank you, Mr. Chairman. Let me say to my colleague from Montana that I appreciate that approach and feel that it is much more practical than that which we endeavored to achieve last night. I was a little bit startled in the arguments from one of the proponents of that bill last night when they were listing the prices of slacks in J.C. Penney's or something. One of the prices that they listed was $2 higher for the foreign slacks, and it struck me that that isn't much of an argument in support of theirs. If you can sell something for $2 more, it doesn't matter to whom the profit goes; it matters that the public prefers that product. And that is not something that can be fixed by protectionism. That was just one of the most bizarre arguments I ever heard.

I recall that 6 or 7 years, Max, that we from livestock-producing States were faced with a peculiarly reverse kind of protectionism in which people from Massachusetts and Missouri and Maine and some other places were trying to limit the export of hides because foreign producers of leather goods would pay more for American hides than domestic producers would. Then, they were complaining at the same time that they could produce that, having shipped it abroad, processed it abroad, and returned it manufactured for less than we could do here. That tells us something. The American cattleman was faced with the worst of both worlds. He could have a limited price on his products and an increased price on his shoes. It was just one of those peculiarly obtuse kinds of protectionism that goes on.

I think the kind of points that you bring up are the kind of points that really must be addressed, but the activities that we indulged ourselves in last night don't do that. They simply miss it, besides all of which, that was significantly among the most racist bills that this Congress has ever passed. If your eyes are round, you are out from under. If you look at the figures, the increases in textiles imports are higher from Britain, from Belgium, and from Italy than they are from the countries that we socked last night. So, the problem is much more complex, and it really comes down to the fact that our eye is on a political master, not an economic master. And I think that if we can focus ourselves, as you tried to do just now, and as I have had in conversations with Ambassador Yeutter that the economic master is a great deal more effective, both in the short run and in the long run, I think we will get somewhere on these very practices that you brought up.

I compliment you, and I thank Ambassador Yeutter again for that list of 227 practices, which tells us that it is not all just a figment of our imagination, but the solution to it is not so simple. The textile and apparel bill is just a bill that seeks to have us denied even products that cost more, simply because they are more appealing for the American consumer. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Moynihan, I apologize. I didn't know that you had come earlier, or I would have put you higher up on the list.

Senator MOYNIHAN. I came to hear the Ambassador, and I welcome him.

Ambassador YEUTTER. No, you really came to arm wrestle with me and win.

Senator MOYNIHAN. We did, but we lost. [Laughter.]

The CHAIRMAN. Senator Chafee.

Senator CHAFEE. I am looking forward to hearing the Ambassador.

The CHAIRMAN. Senator Long.

Senator LONG. I will wait until the Ambassador has presented his testimony. I thank you for coming, Mr. Ambassador, and I will give you the chance to say something before I ask any questions.

Ambassador YEUTTER. All right.

The CHAIRMAN. Mr. Ambassador, we are delighted to have you with us. Go ahead, please.

STATEMENT OF AMBASSADOR CLAYTON YEUTTER, U.S. TRADE REPRESENTATIVE

Ambassador YEUTTER. Thank you, Senator Packwood. It is a pleasure to be back. As you know, this is my first return since my confirmation hearings with all of you. You raised a good many questions and observations and concerns at that time. I certainly tried to respond to those as best I could since then; and what I would like to do now is just spend a few minutes doing a tour of the horizon on what has happened over the last 4½ months; and maybe that can serve as a basis then for moving on into your questions. I will try to do it promptly because I recognize what an intense schedule you are all under at the moment in the Senate.

As you well know, the principal concerns you raised with me during my confirmation hearings was that you were unsure of the trade policy being followed by the administration, either of the existence or adequacy of that policy or the way in which it was being articulated. Whatever the explanation, and I would certainly hope that it was more a question of articulation than a question of existence of adequacy, but whatever the explanation, it seemed to me that it was appropriate that we follow through on your expressions of concerns and begin to intensify our own efforts in that area, communicating not only with you but with the American public and with our trading partners around the world. So, we have spent a lot of time on that, Mr. Chairman, over the last 4½ months, about 18 hours a day, as a matter of fact, because trade has been such a high-profile issue.

I think the committee would appreciate knowing that we probably had at least 25 Cabinet-level discussions of trade since I arrived, several of those in which the President participated personally. As you know, that was followed by four consecutive radio addresses by the President in which trade was the principal topic, and then a major address that he did in the White House, which has received broad distribution, and to which many of you were invited, as well as our private sector advisory committee. We did a so-called white paper at that time, which is by far the most comprehensive enunciation of the policy that we have had in the administration. That has received broad distribution. So, I would hope that by now we have comprehensively articulated what we are all about within the administration in this area. I really believe that we do have a strong sense of direction now, and we have certainly been trying to communicate that sense of direction to our trading partners and to the general public here.

Let me just establish the pillars of the policy very quickly. One has to start with the points that Senator Wallop was making so eloquently here a few minutes ago; and that is the belief that a free and open trading system is in our best interest as a nation; and it is good for America and good for American business and also good for the world. That is the very strong and committed course on which we are embarked within the administration, and we want that fully understood by everyone; and that is a course that will prevail for the next 3-plus years of this administration. We are not going to become protectionists. President Reagan does not have a protectionist bone in his body in my judgment; neither do I. So, certainly, the belief in a free and opening trading system is going to be the cardinal rule of conduct for the administration on trade as far as we can see into the future.

At the same time, we felt it was imperative that we deliver to the world a message that free trade and fair trade must be combined, that one cannot stand alone in one's belief in free and open trade and simply be an observer of the world going by, following a totally different course. We must insist that, if we are to follow a free and open trading course, the rest of the world follow a comparable course. We believe that it is in the interest of our trading partners; but certainly, it would be folly for us to be the only major trading nation of the world committed to a course of free and open trade with the rest of our trading partners taking advantage of us by operating on a course that departs far from that objective. So, we have sent some specific messages in that respect, primarily through the self-initiation of 301 actions. I will not go into the details of those, but you know that we filed a tranch of those at a very early date. We sent that message early on, even before the overall trade messages were sent.

We have done a second tranch of 301 cases since then, and we may well do some more. You referenced our section 303 report with more than 200 barriers to trade, and there are certainly some potential 301 cases among that list. Senator Baucus articulated some of the most provocative of unfair trade barriers that we face, but Senator Baucus, those are just a couple of many. So, we have ample opportunity to make the case for fairer trade and to take an aggressive stance in that regard.

The committee should be able to comprehend at this point that we are clearly following a much more aggressive trade policy than we did months back. That should be clearly evident from the actions we have taken over the last several months. Some of those even involve legislative proposals that have been made to you, including a war chest to deal with the so-called mixed credits issue that has come over to the Hill, with Treasury being the lead on that one.

We are also in the process of evaluating our GSP Program, as you know. That has a termination date for review of January 1987. We clearly have to look closely at the operation of the GSP Program, the provision of duty-free treatment for products flowing in from other nations, and decide where that requires modification because of the conduct of some of the recipient countries. We have had some bilateral strains during this time period, Mr. Chairman, quite a few; some that we precipitated in a sense because we put deadlines on trade issues for the first time in a long time. In my judgment, the United States should use deadlines much more frequently than it does.

We are serious about those deadlines; and that has led to some consternation on the part of our trading partners and some confrontations that might not otherwise have taken place, including retaliation on pasta in our so-called citrus-pasta war on November 1. We have finished, hopefully, a major steel negotiation with the European Community. That was a most important endeavor. There are a few loose ends remaining in that exercise, but most of that negotiation is now wrapped up.

We have a number of other cases that are coming to a head very soon, and you will want to watch those as they proceed because they certainly will give an indication of how we are conducting trade policy and how our trading partners are responding, if at all. Those include a couple of cases with the Japanese with a December 1 deadline, and cases with the European Community with a December 1 deadline, and the so-called Moss process with Japan that will wrap up hopefully at the end of the year.

One of you mentioned the new GATT round. I believe it was Senator Baucus. It is appropriate that we have a brief discussion on that point here because that, too, has a deadline approaching in terms of deciding whether the process will move forward. The annual meeting of the GATT contracting parties will be held in Geneva in about 2 weeks; and at the moment, we are still experiencing a great deal of intransigence from some of our lesser developed country trading partners who are attempting to block progress toward initiation of a new GATT round. In fact, I just read a cable on my way over to this hearing this morning which indicated that several countries, just yesterday, blocked an official report of a senior official's group that was to have been given to the annual meeting later this month. When we have a situation where nations are even blocking reports, that seems to me to be cause for concern; and in my judgment, it is cause for a rather strong and harsh response by the United States and other major trading nations. We simply cannot afford to have a handful of nations with less than 5 percent of world trade dictating the international trading destiny of nations which conduct 95 percent or more of international commerce in this world.

We may well, Mr. Chairman, have a major confrontation ahead of us a few days from now in Geneva. We will keep you informed of the results of that meeting because, if it does turn out—regrettable as that may be—that the meeting will be unproductive and will not lead to establishment of a preparatory committee for a new round, then it is clearly incumbent upon the United States to rethink its international structure and international obligations in light of the structure that we are facing for the conduct of world trade; and we have some hard decisions ahead of us as to how we respond to that particular challenge. That is something that may provoke considerably more discussion between ourselves and the administration and all of you at the Finance Committee relatively soon.

Finally, I should say a word on macroeconomic policy, which many of us think is the heart of the trade issue that confronts us today. Senator Moynihan and I had a considerable interchange on that issue when I was here for my confirmation hearing; and as you know, Senator Moynihan, a lot has been happening on that front since then, too. Secretary Baker, of course, brought together the G-5 Finance Ministers and the central bankers of the G-5 at the Plaza Hotel in New York on September 22 for a meeting that has had international repercussions since then in terms of intervention policies and also in terms of hopefully stimulating a greater conversion of the macroeconomic policies and a lot more coordination of the macroeconomic policies among those nations.

This was followed by the IMF meetings in Seoul, when Secretary Baker also played a leading role in evaluating our LDC debt situation in making some recommendations as to how alterations might be made in that situation. All of that has trade implications, as you well know, because if LDC's do not import, they, are not going to be able to export; and they are not going to be able to service their debt in the long run, even though they may be able to service them in the short run with the kinds of policies that have been imposed by the IMF to date.

It is because of our concern about the export situation, and that clearly is an issue of immense interest; and obviously, the total macroeconomic policy is likewise an issue of interest because of the exchange rate relationships which have prevailed until recently, that is the case of an inordinately strong dollar. As you know, Senator Moynihan, the dollar has come down very significantly in the last couple of months. My judgment is that that will positively affect our trade flows and trade balance as we move into 1986, but probably not until the latter part of 1986; and that is simply because of the lagtimes that are involved and also because, as you well know, nations are going to absorb the differentiation and exchange rates as long as they can before we see concomitant alterations in order books. People just don't change their trading practices overnight unless there is a big economic motivation for that to take place. So, we have some good news coming along on the macroeconomic front, but we should not be unrealistic and expect that to happen overnight because it will not do so.

All in all, though, just summarizing, Senator Packwood, I really believe we have come a long way on a lot of these trade issues over the last 4½ months. We are certainly not there yet. We have a long way to go, but I am quite comfortable with the achievements that we have had in that interim, in that intervening time. It is certainly not all due to efforts by the administration. We have had a very positive attitude on the part of this committee and a lot of other people in the Congress who, with the exception of last night's activities, have resisted the protectionist pressures of the day. And we have had excellent cooperation within the administration and a very forward-looking attitude on many of these very difficult issues.

The one item I haven't mentioned, Senator Packwood, is the question of what might happen in the future legislatively. As you know, we have been working on what I have been calling a legislative initiative, a substantial amount of language on legislative issues such as antidumping subsidies and countervailing duties, intellectual property, the new GATT round, and a number of other issues that we are going to be prepared to share with this committee very soon—probably just within the next few days. That is the kind of positive legislative response to the trade challenges of the day that we would like to see, and I believe many of you share that same objective. And that is showing up now in both the Senate and the House in terms of the packages that are being introduced. Those packages have some elements that we would find troublesome and, in many cases, unacceptable; but the overall thrust of much of the legislation that is being surfaced in both the Senate and the House in the immediate past is affirmative in its scope, as contrasted to the flagrantly protectionist legislation that emerged earlier. So, all in all, Mr. Chairman, I believe the picture looks brighter than it did 4½ months ago in a whole variety of ways; and we hope we can keep it moving in that direction. Thank you, Mr. Chairman.

[The prepared statement of Ambassador Yeutter follows:]

PREPARED STATEMENT OF AMBASSADOR CLAYTON YEUTTER, U.S. TRADE REPRESENTATIVE

Mister Chairman and members of the Committee, I am pleased to appear before you today to discuss America's trade policy. The last time I came before this Committee was for my confirmation hearing last summer, and at that time all of you expressed serious concerns about the sense of direction of our policy. We in the Administration have done a lot since then to respond to those concerns, and I would like to share that response with you. You may properly take credit for stimulating some of it!

At my confirmation hearing, you asserted the need for the United States to take a tougher stance in protecting its international trading interests. You also pointed out the importance of creating a more favorable macroeconomic environment for trade. Many of you were concerned that the Administration did not have a coherent trade policy, and I promised I would provide you at an early date a clear and forceful articulation of that policy.

Since that hearing, the Administration has devoted an enormous amount of time and energy to the consideration and development of policies to deal with America's trade challenges. The Cabinet has taken up various trade issues on some 25 different occasions in the past four months, and trade has been an almost constant topic of action and discussion at the Subcabinet level.

Although we still have a lot of work to do, I believe those efforts have started to pay off. Notably:

The President has clearly and boldly outlined the Administration's trade policy objectives and released an action plan for realizing those objectives.

The Administration has asserted to the rest of the world in unmistakable terms that we are determined to create a "level playing field" for U.S. business firms. This message has been most forcefully conveyed by our self-initiation of Section 301 cases and targeted mixed credit export financing offers.

In conjunction with our principal trading partners, we have begun major initiatives to promote stronger and more balanced international economic growth, with much improved coordination of macroeconomic policies.

With that brief overview, I would now like to set out for you in greater detail the numerous and varied actions the Administration has taken to alleviate our trade difficulties and to restore a sense of fairness and equity to the international trading system.

THE ADMINISTRATION'S TRADE PROGRAM

On September 23, the President announced a comprehensive set of proposals for deling with America's trade problems. The principles underlying the Administration's program are set out in detail in the Administration's "Statement on International Trade Policy" which I hereby submit for the record.

First and foremost, the President remains committed to a policy of free and fair trade. Such a policy is the best way to ensure that America attains its full economic potential. An open and fair trading system globally will produce jobs and exports, improve the use of our nation's resources, promote more rapid economic growth and innovation and result in higher incomes and living standards for all Americans. Let there be no doubt about our commitment to that course. President Reagan is not a protectionist and never will be, and neither will I. The Administration's gyroscope on trade is spinning properly, in my judgment, and will continue to do so for the next three years.

Protectionism would destroy the economic vitality of America's economy. It would stifle competition, retard innovation, reward the inefficient, cost jobs, invite retaliation and lower America's standard of living. It is a policy we as a nation cannot afford.

Instead, the United States must continue to play its critical role in promoting a more open and equitable world trading system. Without doubt the present system has a multitude of imperfections and inequities. But that doesn't mean we should just give up! History has shown that periods of trade liberalization lead to increased economic growth, and trade restrictions lead to economic inefficiencies. The international community has made enormous progress in reducing traditional trade barriers during the past 40 years. During those four decades, growth in world trade has outpaced and in fact has driven the growth in global production. America's self interest, and that of other nations as well, lies in maintaining and improving the international trading system that has evolved since World War II.

The Administration's policy is to take action, either singly or in concert with our trading partners, to renew and restore this system. We will continue to pursue more open markets overseas while opposing actions at home and abroad which restrict or distort trade.

Based on these guiding principles, the Administration has developed a three-pronged plan to address America's trade problems. Our plan is to ensure that free trade is also fair trade, to strengthen and revitalize the international trading system and to alleviate the macroeconomic causes of our trade deficit.

A. UNFAIR TRADE

While supporting free trade, the Administration is also committed to a policy of fairness and equity in international trade. The United States must and will act to protect its own trading interests. We will not tolerate foreign actions that discriminate against American business or which rob us of legitimate returns on our investments in such areas as research and development.

We intend to make it absolutely clear to other nations that they cannot deny fair market access to U.S. exporters and continue to sell their products freely in the United States. This is not the 1970s when we regularly ran a trade surplus; this is the 1980s and we have a $150 billion trade deficit! We can no longer afford to stand by and allow other countries to routinely deny our goods and services equitable access to their markets. The Administration, therefore, will aggressively seek to open foreign markets to American exports. If nations are to operate in and benefit from a global marketplace, then their markets must also be open.

The Administration has taken the unprecedented step of self-initiating Section 301 unfair trade cases against such countries as Brazil, Korea and Japan, and has accelerated ongoing cases against the EC and Japan. We are also initiating GATT proceedings against EC export subsidies on wheat.

Our objective is to obtain the elimination of unfair foreign trade practices through consultations and negotiations. When necessary, however, we will not hesitate to retaliate against the perpetrators of such practices. An example is the President's decision to impose a 25 percent to 40 percent tariffs on pasta imports from the European Community to compensate for the injury to U.S. citrus exports caused by EC preferences to Mediterranean countries.

This determination to deal effectively with foreign unfair trade practices is already beginning to show results. For example, we recently reached agreement with Taiwan to eliminate their long-standing barriers to U.S. exports of beer, wine and tobacco products.

One area to which the Administration is paying particular attention is that of intellectual property. The future competitiveness of U.S. industry is very much a function of our ability to reap the benefits of our technological advances. Encouraging the development of technology and creative works, as well as enhancing trade, requires more than just removing trade barriers. We must actively promote the expansion of trade by enhancing security and assuring rewards to the creators and owners of intellectual property.

Over the past several months, we have held consultations and negotiations with our trading partners whose conduct in this area concerns us most. These include Taiwan, Singapore, Korea and Mexico. The problems in Korea has been particularly troublesome, and thus far there has been virtually no progress in our talks with that country. As a result, the President directed me to launch a Section 301 investigation into the adequacy of Korean laws governing the protection of intellectual property.

The first tranches of Section 301 actions represent only the initial step in our efforts to ensure that trade is both free and fair. We will launch additional actions if and when we deem it appropriate to do so.

As you know, we have just completed an extensive study of foreign trade barriers, in accordance with Section 303 of the Trade and Tariff Act of 1984. The report, which was made available to you two weeks ago, describes foreign trade and investment barriers and distortions by country. It examines 12 categories of barriers: tariffs and other import charges: quantitative restrictions; import licensing; customs barriers; standards, testing, labeling and certification procedures; government procurement; export subsidies; inadequate intellectual property protection; countertrade and offsets; barriers to services trade; investment restrictions and other trade barriers, such as industrial targeting.

As I indicated in my letter of transmittal accompanying the report, the information contained in it was used by the administration to develop some of the specific unfair trade initiatives undertaken over the past few months. We will continue to consult the report as we design appropriate actions to combat other unfair foreign trade practices. We will also use it in setting priorities and objectives for a new GATT round of trade talks, as well as in various bilateral negotiations.

The report covers "significant" barriers to trade. It makes no attempt to identify which barriers are "unfair." Indeed, many of the measures identified in the report (tariffs, e.g.), while significantly impeding U.S. exports, may be fully consistent with the rules of international trade. Certain other measures described in the report may require GATT consideration before one can determine whether or not they are consistent with GATT rules. And in some instances, such as trade in services, intellectual property and investment, there are no GATT rules on which to base a present judgment. Nevertheless, whether a barrier is legal, illegal or not covered by the GATT, if it is damaging to U.S. interests we should attack it. We'll do so in bilateral discussions and negotiations, and hopefully also in a new GATT round.

The President has also established, under the direction of Secretary of Commerce Baldrige, an interagency Strike Force to identify unfair trade barriers and recommend actions to eliminate our Section 303 report to determine which foreign trade barriers are most adverse to our trading interests, and to consider and recommend appropriate action to do away with those barriers.

In addition to the Administration's action on unfair trade barriers, we are also accelerating our efforts to address the problem of foreign predatory financing which in recent years has denied U.S. exporters important overseas sales. The President has proposed to Congress a $300 million fund to support up to $1 billion in export financing. The purpose of this funding is to increase American leverage in negotiations to eliminate predatory tied aid credit financing. The fund will be used to capture both traditional and new export markets of those countries who use this form of financing and have been intransigent in the negotiations.

The Administration is also in the process of reviewing the competitiveness of all beneficiary developing countries participating in the Generalized System of Preferences (GSP) program to determine the level of future benefits to be accorded these countries. In making that determination the President will consider a country's level of development, its competitiveness and its practices. Among the practices the President will be looking at are the openness of the country's market to foreign goods and services, its policies towards international investment, the degree of protection it affords intellectual property, and its regard for international workers' rights.

As part of our general review of trade policy, the President has expressed a desire to work with the Congress to put into place legislation that would help us promote free and fair trade. In line with this, the Administration is reviewing proposals for changes in and additions to U.S. trade laws. The proposals include: new trade negotiating authority, revisions to our laws protecting intellectual property, export promotion initiatives, proposals to improve access of our telecommunications firms in foreign markets, and various technical amendments to our trade laws. We will share our views on all these legislative issues with the Congress in the very near future.

It is important to remember that even fairly-traded goods can have a significant effect on American business. That is why we have "safeguard" provisions under GATT Article XIX and under Section 201 of our own trade laws. Both provide for temporary import restraints, under certain prescribed conditions, to allow domestic industries time to adjust to changes in international competition.

Some have suggested that Section 201 does not provide adequate protection for U.S. industries—because the Administration is unwilling to use it. The record demonstrates otherwise. Eleven Section 201 cases have been filed since the Administration took office. Of those eleven cases, the International Trade Commission found no injury in six. Of the five remaining cases, the President granted import relief in two—to heavyweight motorcycles and specialty steel. In the case of carbon steel, the President took alternative action to resolve the problem. Only in two cases—copper and footwear—did the President reject import relief. In the copper case, many more copper fabricators' jobs would have been lost than miners' jobs saved. In the footwear decision, the industry failed to show that relief would have improved their international competitiveness. In both cases, the President directed the Secretary of Labor to develop special plans to help workers adjust to import competition. This seems to me to be an impeccable record in administering Section 201, rather than one subject to criticism.

The Administration has also proposed more permanent measures to deal with shortcomings in the international trading system and the overall trade deficit.

B. A NEW ROUND OF MULTILATERAL TRADE NEGOTIATIONS

In order to permanently eliminate or reduce unfair foreign trade practices and increase foreign market access for U.S. exporters, it is imperative that we launch a new round of multilateral trade negotiations. During the past four decades, the General Agreement on Tariffs and Trade, or GATT, has served the world well as a framework for international trade negotiations and the conduct of international commerce. Under GATT auspices, successive rounds of multilateral trade negotiations have led to substantial trade liberalization and an enormous increase in global trade.

But the discipline imposed on international trade by the GATT has been crumbling. The postwar international consensus on a basic framework for international trade has reached the breaking point under the combined pressures of global recession, debt crises, fluctuating energy prices and volatile exchange-rate movements. The need to restore discipline to international trade is one of the fundamental reasons we need a new trade round.

Moreover, the world has changed dramatically since the GATT was first formed, and it is time the GATT changed as well. Services have become more important in international trade, but there are few rules governing them. Major investment issues have evolved since the last round of trade negotiations. And we need much stronger rules on intellectual property, for research and development is the foundation for many of our high technology industries. In addition, Tokyo Round codes were only a first step toward non-tariff measure discipline in such areas as subsidies, government procurement and dispute settlement. Finally, we need to bring agricultural trade under the auspices of the GATT in a truly meaningful way for the first time.

For their own reasons, a number of our fellow GATT members have been unenthusiastic about a new round of multilateral negotiations. They prefer not to have international rules in new areas such as services, because the present situation gives them the privilege of being essentially as restrictive as they wish. Fortunately, an overwhelming majority of the GATT membership recognizes that there is no "free lunch" in international trade, and that even the developing nations must make at least some concessions in order to receive benefits. In fact, if the position of the LDCs who oppose a new GATT round were to prevail, those same LDCs would belatedly discover that they have hampered their own economic growth by restricting their own export opportunities. That makes no sense, of course, and that is why the United States took the unprecedented step in September of calling for a special session of the GATT to discuss a new trade round.

In that endeavor we were supported by 65 of the 90 GATT members. The outcome of the session was favorable. The preparatory process for a new round was officially begun, and a report of a Senior Officials Group will be made at the annual meeting of the GATT Contracting Parties starting November 25. We are hopeful that a Preparatory Committee will then be established to begin work on a negotiating agenda for the new round, and that a Ministerial meeting to launch the negotiations can take place in mid-1986.

It is possible that these efforts will not bear fruit in Geneva. Should such a highly unfortunate result develop, we are prepared to use alternative ways of bringing about a more free and open trading system. We could, for example, convene a conference here in Washingon to negotiate on trade matters of interest to the participants only. Those attending would be countries which share our objectives of seeing trade disciplines and codes of conduct established in such areas as services, intellectual property and other mutually-agreed subject matter. Nonparticipants would not enjoy any of the benefits of such international agreements.

We would, of course, retain the means to defend our trade interests, including greater use of our self-initiation authority under Section 301. This Administration will not permit a small number of inward-looking nations, representing a nominal percentage of world trade, to control the trading destiny of nations which conduct 95 percent or more of the world's commerce.

I would welcome the Committee's input on this scenario as it unfolds.

The United States is committed to GATT and the multilateral negotiating process. Nevertheless, such negotiations are not an end in themselves; now will the United States be held hostage to the multilateral negotiating process. That process is clearly the preferred way for the United States and other nations to achieve the crucial goal of increased economic growth through expanded world trade. But there are other ways as well. For example, the Administration is prepared to negotiate on a plurilateral or bilateral basis with like-minded nations. This path would become all the more important and urgent if the movement towards a new trade round is stalled in Geneva this month at the Contracting Parties annual meeting.

An example is the recently concluded free trade area with Israel. As you know, we are now in the process of discussing a similar arrangement with one of our most important trading partners, Canada. Canadian Prime Minister Mulroney has proposed that we consider bilateral trade negotiations on the "broadest possible package of mutually-beneficial reductions in barriers to trade in goods and services."

President Reagan has welcomed the Canadian proposal, and he believes it offers an historic opportunity for both nations. It is rare indeed for two of the largest trading nations of the world to offer to open their borders to each other. If we can successfully conclude such a negotiation, it could dramatically enhance the growth opportunities of both countries as they enter the next century.

Before we commence negotiations we will, of course, consult with this Committee and other interested Members of the Congress, and with our private sector advisory committees. Some Members have already suggested that we delay free trade negotiations until our present bilateral disputes are behind us. But with the volume of trade that flows between the United States and Canada, we will always have bilateral disputes. We should not permit those transitory frustrations to blur the importance of improving long-term trade relationships and opportunities.

C. MACROECONOMIC INITIATIVES

Finally, and perhaps most importantly, the Administration has taken a number of steps to create an economic climate more favorable to U.S. trade. Chief among these are attempts to achieve increased and more balanced growth at home and abroad.

Even if all the world's trade barriers, unfair or fair, were eliminated, the United States would still have a large trade deficit. The strong dollar—resulting from the strength of the U.S. economy, excessive federal spending and foreign confidence in our political and economic system—has reduced American export competitiveness over the past several years and has severely stressed our import-sensitive industries. This, of course, has provoked the political turmoil of recent months which has been felt by both the Congress and the Administration.

We are attempting to respond to this macroeconomic challenge in a decisive way, both with respect to what we in the United States can do to ameliorate the situation, and what our major trading partners can do.

A significant step was taken when Secretary of the Treasury James Baker met with his counterparts from Britain, France, Germany and Japan in September. They agreed on measures to promote stronger and more balanced growth among our respective economies, and the subsequent actions have already helped strengthen other currencies relative to the dollar. The dollar has declined 15 percent vis-a-vis the Japanese yen and eight percent vis-a-vis the German mark since September.

The actions announced by the G-5 are not a one-shot affair but are one step in a continuing process. We must also make the hard decisions here at home needed to reduce the dollar's value. The starting point must be to cut the Federal budget deficit by reducing excessive government expenditure. We also need enactment of a tax reform proposal that will encourage private savings and investment.

The problem of the debt crisis in developing countries also needs to be addressed. U.S. exports to "high-debt" developing countries have fallen dramatically in recent years. For example, between 1981 and 1984, there was a shift in our net trade balance with six debt-burdened Latin American countries from a $4.4 billion surplus to a $16.2 billion deficit.

As Secretary Baker pointed out at the IMF meetings is Seoul, it is essential that these countries adopt more market-oriented policies, thereby improving their economic performance. To this end, we believe that greater emphasis must be placed on reducing trade and investment barriers as part of a comprehensive effort, including the international lending institutions, to establish the fundamental conditions for sustained growth in developing countries. These nations must ultimately import more—especially in capital and technology—if they are to export more. If they are responsive, and make a concerted effort to get their own economic houses in order, then the private business community and applicable lending institutions should respond positively, too. We need to bring these LDC economies to life, not bury them.

CONCLUSION

As you can see, we've done a lot of work on trade policy in recent weeks. We in USTR have had splendid cooperation from other government agencies in this endeavor, and from the relevant Congressional committees as well. The United States now has what I believe to be a coherent, comprehensive trade policy and trade strategy. We have made large strides in a short period of time, but we still have a long way to go. Our trade problems, and the political strains which accompany them, are by no means behind us. President Reagan and I look forward to working with you in our common desire to ensure that American and foreign firms play by the same rules in international trade and that both reap the benefits of a free and fair trade policy.

TEXT OF REMARKS BY THE PRESIDENT TO BUSINESS LEADERS AND MEMBERS OF THE PRESIDENT'S EXPORT COUNCIL AND ADVISORY COMMITTEE FOR TRADE NEGOTIATIONS

(East Room, the White House, Sept. 23, 1985)

I am pleased to have this opportunity to be with you to address the pressing question of America's trade challenge for the eighties and beyond.

Let me say at the outset that our trade policy rests firmly on the foundation of free and open markets—free trade. I, like you, recognize the inescapable conclusion that all of history has taught: the freer the flow of world trade, the stronger the tides for human progress and peace among nations.

I certainly don't have to explain the benefits of free and open markets to you. They produce more jobs, a more productive use of our Nation's resources, more rapid innovation and a higher standard of living. They strengthen our national security because our economy, the bedrock of our defense, is stronger.

I am pleased that the United States has played the critical role of insuring and promoting an open trading system since World War II. And I know that if we ever faltered in the defense and promotion of the worldwide free trading system, that system will collapse to the detriment of all.

But our role foes not absolve our trading partners from their major responsibility to support us in seeking a more open trading system. No nation, even one as large and as powerful as the United States, can, by itself, insure a free trading system. All that we and others have done to provide for the free flow of goods and services and capital is based on cooperation. And our trading partners must join us in working to improve the system of trade that has contributed so much to economic growth and the security of our allies and of ourselves.

And, may I say right here, to you leaders of industry that my admiration for business in the United States is stronger than ever. You know sometimes in Washington there are some who seem to forget what the economy is all about. They give me reports saying the "economy" does this and the "economy" will do that, but they never talk about business. Somewhere along the way those folks in Washington have forgotten that the economy *is* business. Business creates new products and new services. Business creates jobs. Business creates prosperty for our communities and our nation as a whole. And business is the people that make it work—from the C.E.O. to the workers in our factories.

I know too that American business has never been afraid to compete. I know that when a trading system follows the rules of free trade, when there is equal opportunity to compete, American business is as innovative, efficient and competitive as any in the world. I also know that the American worker is as good and as productive as any in the world.

And that is why to make the international trading system work, all must abide by the rules—all must work to guarantee open markets. Above all else, free trade is, by definition, fair trade.

When domestic markets are closed to the exports of others, it is no longer free trade.

When governments subsidize their manufacturers and farmers so that they can dump goods in other markets, it is no longer free trade.

When governments permit counterfeiting or copying of American products, it is stealing our future, and it is no longer free trade.

When governments assist their exporters in ways that violate international laws, then the playing field is no longer level—and there is no longer free trade.

When governments subsidize industries for commercial advantage and underwrite costs, placing an unfair burden on competitors, that is not free trade.

I have worked for 4 years at Versailles and Williamsburg and London and Bonn to get our trading partners to dismantle their trade barriers, eliminate their subsidies and other unfair trade practices, enter into negotiations to open markets even further, and strengthen GATT, the international accord that governs worldwide trade. I will continue to do these things.

But I also want the American people and our trading partners to know that we will take all the action that is necessary to pursue our rights and interests in international commerce under our laws and the GATT, to see that other nations live up to their obligations and their trade agreements with us.

I believe that if trade is not fair for all, then trade is "free" in name only.

I will not stand by and watch American businesses fail because of unfair trading practices abroad. I will not stand by and watch American workers lose their jobs because other nations do not play by the rules.

We have put incentives into our own economy to make it grow and create jobs. And, as you know, business has prospered. We have created over 8 million new jobs in the last 33 months. Just since 1980, manufacturing production has increased 17 percent.

But I am not unmindful that within this prosperity some industries and workers face difficulties. To the workers who have been displaced by industrial shifts within our society we are committed to help.

To those industries that are victims of unfair trade, we will work unceasingly to have those practices eliminated.

Just a few weeks ago I asked the United States Trade Representative to initiate unfair trade practice investigations, the first time a President has done this. And, as you know, we have self-initiated three such cases that will investigate a Korean law that prohibits fair competition for U.S. insurance firms, a Brazilian law restricting the sale of U.S. high technology products, and Japanese restrictions on the sale of U.S. tobacco products. I also have ordered the United States Trade Representative to accelerate the ongoing cases of Common Market restrictions of canned fruit, and Japanese prohibitions on imports of our leather and leather footwear.

But I believe more must be done. I am, therefore, today announcing that: I have instructed Ambassador Yeutter to maintain a constant watch and to take action in those instrances of unfair trade that will disadvantage American businesses and workers; I have directed the Secretary of the Treasury to work with the Congress to establish a $300 million fund that will support up to a billion dollars in mixed credit loans. These funds will counter our loss of business to trading partners who use what, in effect, are subsidies to deprive U.S. companies of fair access to world markets. And, I have asked that these initiatives be continued until unfair credit subsidies by our trading partners are eliminated through negotiations with them.

I have further instructed Treasury Secretary Jim Baker to inform the participants at the International Monetary Fund and World Bank conferences in Seoul that we will take into consideration the trading practices of other nations in our deliberations and decision-making.

A major factor in the growth of our trade deficit has been the combination of our very strong economic performance and the weak economic performance of our major trading partners over the last 4 years. This has limited our exports and contributed to the weakening of other currencies relative to the dollar, thereby encouraging additional imports by the United States and discouraging our exports.

Yesterday I authorized Treasury Secretary Baker to join his counterparts from other major industrial countries to announce measures to promote stronger and more balanced growth in our economies and thereby the strengthening of foreign currencies. This will provide better markets for U.S. products and improve the competitive position of our industry, agriculture, and labor.

I have ordered the Secretary of State to seek time limits on negotiations underway to open up markets in specific product areas in Japan.

I have instructed the United States Trade Representative to accelerate negotiations with any and all countries where the counterfeiting and piracy of U.S. goods has occurred to bring these practices to a quick end. And I look forward to working with the Congress to increase efforts to protect patents, copyrights, trademarks and other intellectual property rights.

And, finally, I am today directing that a strike force be established among the relevant agencies in our Government whose task it will be to uncover unfair trading practices used against us and develop and execute strategies and programs to promptly counter and eliminate them.

I am also looking forward to working with the Congress to put into place any necessary legislation that would help us promote free and fair trade and secure jobs for American workers. Among the topics that we should jointly consider are:

Authority to support our new trade negotiating initiatives that would, among other things, reduce tariffs and attempt to dismantle all other trade barriers.

To protect intellectual property rights including trade in articles that infringe U.S. process patents, longer terms for agricultural chemicals, and eliminating Freedom of Information Act abuses that will help our businesses protect their proprietary property.

To improve our anti-dumping and countervailing duty laws so that a predictable pricing test covers non-market economies enabling our companies to have protection against unfair dumping from those countries. We should also improve these laws so that business can have full and rapid protection in receiving help against unfair imports.

To amend our trade laws to put a deadline on dispute settlement and to contain a fast track procedure for parishable items. We should no longer tolerate 16-year cases, and settlements so costly and time-consuming that any assistance is ineffective.

I am also directing the Secretary of Labor to explore ways of assisting workers who lose jobs to find gainful employment in other industries. I look forward to working with Congress in this vital task.

Additionally, I welcome the suggestions of the Members of Congress on other potential legislation that has as its object the promotion of free and fair trade. I will work with them to see that good legislation is passed. Conversely, I will strongly oppose and will veto measures that I believe will harm economic growth, cause loss of jobs and diminish international trade.

But, I do not want to let this discussion pass without reminding all of our ultimate purpose—the expansion of free and open markets everywhere. There are some, well-meaning in motive, who have proposed bills and programs that are purely protectionist in nature. These proposals would raise the costs of the goods and services that American consumers across the land would have to pay. They would invite retaliation by our trading partners abroad, would in turn lose jobs for those American workers in industries that would be the victims of such retaliation, would rekindle inflation, would strain international relations, and would impair the stability of the international financial, and trading systems.

The net result of these counter-productive proposals would not be to protect consumers or workers or farmers or businesses. In fact, just the reverse would happen. We would lose markets, we would lose jobs and we would lose our prosperity.

To reduce the impediments to free markets, we will accelerate our efforts to launch a new GATT negotiating round with our trading partners, and we hope that the GATT members will see fit to reduce barriers for trade in agricultural products, services, technologies, investments, and in mature industries. We will seek effective dispute settlement techniques in these areas.

But if these negotiations are not initiated or if insignificant progress is made, I am instructing our trade negotiators to explore regional and bilateral agreements with other nations.

Here at home we will continue our efforts to reduce excessive government spending and to promote our tax reform proposal that is essential to strengthening our own economy and making U.S. business more competitive in international markets.

Further, we will encourage our trading partners, as agreed upon at the Bonn Summit, to accelerate their own economic growth by removing rigidities and imbalances in their economies. And we will urge them to provide sound fiscal and monetary policies to have them fully participate in the growth potential that is there for all.

We will seek to strengthen and improve the operation of the international monetary system, and, we will encourage the debt burdened less-developed countries of the world to reduce and eliminate impediments to investments, and eliminate internal restrictions that discourage their own economic growth.

Let me summarize. Our commitment to free trade is undiminished. We will vigorously pursue our policy of promoting free and open markets in this country and around the world. We will insist that all nations face up to their responsibilities of preserving and enhancing free trade everywhere. But let no one mistake our resolve to oppose any and all unfair trading practices. It is wrong for the American worker and American businessman to continue to bear the burden imposed by those who abuse the world trading system.

We do not want a trade war with other nations; we want other nations to join us in enlarging and enhancing the world trading system for the benefit of all.

We do not want to stop other nations from selling goods in the United States; we want to sell more of our goods to other nations.

We do not dream of protecting America from others' success; we seek to include everyone in the success of the American dream.

Administration Statement on International Trade Policy

(September 23, 1985)

THE ADMINISTRATION'S BASIC TRADE PRINCIPLES

A policy of free and fair trade is in the best interest of the citizens of the United States and the world. Such a policy produces more jobs, improves the use of our nation's resources, promotes more rapid growth and innovation, and ensures a higher standard of living for Americans. Free and fair trade also advance our national security interests by strengthing the economic and political systems of our developed and developing country trading partners.

Despite these clear net benefits, pressures for protectionism persist and have been on the rise in recent years. Protectionism is costly and inimical to our nation's economic prosperity and security interests. Protectionist proposals for import surcharges or quotas, whether or not made for the purpose of political gain, are irresponsible and dangerous.

The United States plays the critical role in ensuring and promoting an open worldwide trading system. If the United States falters in the defense and promotion of a more open worldwide trading system, the system will be in danger of collapse, adversely affecting our national well-being.

The international trading system is based upon cooperation. Thus, our trading partners also have a major obligation to support a more open trading system. This obligation includes: dismantling trade barriers, eliminating subsidies and other forms of unfair trade practices and entering into trade liberalization negotiations in the GATT. Since World War II, we have made significant progress in moving toward an open worldwide trading system. Protectionism threatens to undermine that system. Our trading partners must join us in working to improve the system of trade that has contributed to the economic growth and security of ourselves and our allies.

America has never been afraid to compete. When trade follows the rules, and there is an equal opportunity to compete, American business is as competitive as any. This is fair trade and we will not impair it. When these conditions do not exist, it is unfair trade, and we will fight it.

In its 1981 Statement on U.S. Trade Policy, the Administration indicated the high priority it would give to international trade. It emphasized the duel objectives of strengthening our private sector through the President's domestic economic recovery program and by pursuing open and fair trade internationally. Since then, real private investment has risen more rapidly than GNP, particularly in the case of producers' durable equipment, and now real plant and equipment investment accounts for a higher share of national output than at any other point in post-war history. This activity indicates that U.S. industry is re-equipping with the most modern and productive technologies available and is building a solid base to strengthin its long-run competitive position.

The Administration's basic policy approach has been to allow the operation of private market forces to the maximum extent possible. The results of this approach have been highly beneficial. Since 1980, private civilian employment has grown by 8 million. Manufacturing production has increased by 17 percent. Meanwhile, our nation's price inflation has dropped from double-digit levels (12.4 percent in 1980) to less than 4 percent. Ongoing efforts to strengthen our domestic economy through the restoration of noninflationary growth will help further strengthen our economy's performance in coming years and improve our international competitiveness.

Internationally, the Administration has stepped up efforts for a more open and fair system of global trade, in which market forces operate free from government restrictions and subsidies. The Administration has sought to reduce foreign barriers to U.S. exports, to counter foreign subsidy and other unfair practices abroad, and to use our legal authority to encourage our trade partners to live up to their obligations.

We continue to belive that open markets, based upon mutually agreed rules and equitable trading relations, are in our national interest.

CHALLENGES OF EXPANDING INTERNATIONAL TRADE

The U.S. economy is becoming more integrated with the global economy. Our businesses, workers and various levels of government must increasingly take into account this fundamental fact. In 1985, U.S. exports and imports of goods and sevices will consitute approximately 21 percent of our gross national product. This compares with 13 percent in 1970 and only 9 percent in 1950.

The trend toward a greater role for international trade in our economy is irreversible. Rapid growth and change in the economies of other countries, both developed and developing, provide new and growing markets for our exports and sources of our imports. As a result, U.S. production and consumption activities are becoming more integrated with those located abroad.

The growing dependence on foreign markets of our industrial and agricultural producers, and the important challenge of foreign competition in our domestic market, make it imperative that we continue to foster a strong and internationally competitive domestic economy and a more open global system for trade and capital flows. This Administration accords a high priority to policies that achieve these objectives.

Accompanying the growing importance of international markets to our economy are increasing major threats to open and market-based trade. Extensive government intervention in the economies of our trading partners impair or ability to do business internationally. This Administration will continue to seek vigorously the liberalization of trade, industrial, agricultural, intellectual property, and investment policies overseas to enable our producers to increase exports and foster U.S. growth and jobs.

We must also address protectionist pressures at home. Advocates of import surcharges or other forms of protection frequently cite our large trade deficit as an argument for restricting imports. They argue that our trade deficit is a drag on domestic economic growth. Yet, such an analysis is as wrong as its prescriptions. Protectionism simply benefits some industries at the expense of the rest of the economy. Fewer imports are offset by fewer exports; but the trade balance is not improved on more than a temporary basis. Protectionism drives up costs to consumers and misallocates resources within the economy. It also sets in motion a trade war psychology of retaliation and further market restrictions.

The best proof that free markets and free trade work is our own recent growth rate compared to the slower growth of the economies of our trade partners. Our trade deficit has become large; but at the same time, 8 million jobs have been created since 1980. Our robust growth over the last several years has stimulated demand for both domestic and foreign products. We must recognize that we could not have had our own vibrant growth without also creating a greater demand for imports. The availability of imports has served our interest by giving Americans greater choice and lower prices, and by helping to keep friendly nations economically stable.

In contrast to the robust economic growth and rising demand in the United States over the last several years, the growth of our trade partners has been generally slower. The wide differential between our growth and that of our trading partners has further contributed to our trade deficit (and our trade partners' surpluses). While our nation's industrial production has grown by 19 percent since 1982, the industrial output of our major developed country partners generally has grown much less—by 17 percent in Canada, by 2.5 percent in France, by 8 percent in Germany, by 9 percent in Great Britain, and by 1.4 percent in Italy. In contrast to the 8 million jobs created since 1980 in our country, there has been no net increase in employment in Europe for more than 10 years. Greater private investment spending in these and other countries would help close the gap between their growth and employment rates and ours. This, in turn, would help shrink our trade deficit by increasing foreign demand for our products relative to our demand for their products.

The international debt problems of many developing nations have cut into their ability to import from the United States. U.S. exports to highly-indebted developing countries in some cases have been cut by half since 1981. As these debtor nations adopt policies that shift their economies away from government-controlled to market-oriented decision making, and as they regain the confidence of the international business and banking community, their potential to grow will be restored and U.S. exports will once more expand to them.

The Administration will encourage debt-burdened LDCs to reduce government impediments to the functioning of markets in their economies, encourage production through market incentives to their business firms and employees, and substitute equity capital for debt by encouraging both domestic and foreign investment. These steps will enhance economic growth, thereby increasing debt service capabilities and re-establishing U.S. export opportunities.

THE DOLLAR IN INTERNATIONAL MARKETS

Since 1978, the dollar has risen substantially in value relative to the values of the currencies of our major industrial trading partners. Its rise has been fueled by an increased demand for dollar-denominated assets worldwide, reflecting the strong growth prospects and safety of investment in the U.S. economy. These capital flows have added to our productive resources and have helped to put a lid on inflation.

The increase in the dollar's value, while enriching our economy, has also placed additional impediments in the way of our exports and has acted to encourage imports. The Administration is concerned about the effect of the dollar's rise in value on our ability to compete internationally. Many U.S. producers have become less competitive relative to their competitors overseas because of the dollar's increase in value over the past 7 years. There are, however, no quick fixes for this situation. We should avoid attempting to limit the inflow of capital which seeks to take advantage of, and contributes to, the positive prospects for our economic growth. The dollar's strength, in part, reflects the relative strength of our economy.

An important contribution to moderating the dollar's rise would occur if the policies of our trade partners succeeded in accelerating the growth of their economies. This would importantly contribute to the growth of U.S. exports through both a gradual strengthening of their currencies and the effect of their expanded incomes on their purchase of U.S. products. The Administration is encouraging our trade partners to adopt policies that will accelerate their economic growth, and will urge Bonn Summit participants to act on their commitments to remove domestic rigidities and imbalances in their economies. We are not seeking old-fashioned "pump-priming" increases in government spending or inflationary monetary policies, but rather policy shifts such as expenditure and tax reductions, resource reallocation and financial market liberalization which would permanently increase growth opportunties.

FEDERAL EXPENDITURE, TAX AND REGULATORY POLICIES

The Administration's economic recovery program has provided incentives to invest, increase productivity and diminish inflation from the dangerously high levels reached in 1979 and 1980. The resulting reduction in interest rates, coupled with lower marginal tax rates for individuals and businesses, have encouraged investment and yielded a strong recovery with lower inflation.

The expansion of plant and equipment investment since 1982 has been the most rapid of any economic recovery in the postwar period. Investments being made today will result in long-term enhanced U.S. competitiveness both in our overseas and domestic markets.

It is important to our international competitiveness to maintain, under our tax policies, the stimulus to saving and investment. The Administration has retained, as part of its tax reform proposal, the elements of our tax code that are favorable to individual and business saving and capital investment—including reduced individual and corporate tax rates, indexed depreciation of assets, and the tax credit provision for research and development expenditures. The President's tax reform proposal is essential to strengthening the economy and making U.S. businesses more competitive in international markets.

Another major Administration initiative—to reduce federal expenditures—is also important to the improvement of our international competitiveness through a moderation of the dollar's value and the reduction of the claims that such expenditures place on the nation's resources. Government spending, whether financed by taxes or borrowing, drains resources from the private sector, requiring the importation of many billions of borrowed capital funds and contributing to raising the value of the dollar.

The high level of federal government expenditures also has other negative effects on our nation's international competitiveness. It has prevented interest rates from being further reduced. Unless government expenditures are brought back in line with historical levels, resources will be diverted from expanding investments in the private sector. The American business community has repeatedly indicated that the financial cost of capital is a major problem for U.S. companies competing in world markets. We must bring interest rates down further by reducing federal government spending.

The Administration has made great efforts to persuade the Congress to reduce federal expenditures substantially. Such reductions would not only benefit our domestic economy, but also substantially improve our international competitive standing. Interest rates could be further reduced, more resources would be released to more productive uses in the private sector; and, very importantly, we would expect to see a change in the level of the dollar that would benefit U.S. export and import-competing industries. We must recognize, however, the possibility that a reduction in the government budget deficit may not lead to a rapid and substantial decline in the value of the dollar, particularly if domestic and foreign investors perceive such an accomplishment as further increasing the attractiveness of U.S. assets. Nevertheless, tighter control over federal expenditures and greater public sector efficiency would improve the performance of the economy and our international competitiveness.

The Administration is also committed to work to reduce the burden of federal regulations that unnecessarily hamper U.S. Economic growth, productivity and exports. On the export side, the Administration sought and obtained legislation in the form of the Export Trading Company Act of 1982, allowing banks to participate actively in the formation of export trading companies to facilitate U.S. exports of goods and services. The Administration will continually review the operation of this Act, and propose further modifications if there is a need to do so.

In the domestic regulatory area, introducing more competition into previously regulated sectors will increase productivity and our international competitiveness. The Administration will also consider trade implications when reviewing proposed regulations and when developing further deregulation initiatives. We will examine the use of the trade leverage created by its deregulatory process to seek to open foreign markets, thereby minimizing the problem of free rides for foreign suppliers.

Increasingly, the international competitiveness of U.S. Industries depends upon the protection of U.S.-generated intellectual property (patents, copyights and trademarks). The Administration will increase efforts to protect U.S.-generated intellectual property; we will accelerate on-going work in this critically important area with a view toward possible Administration legislative and administrative initiatives. In a related area, the Administration is implementing an important new program aimed at increasing the rate of commercialization of new products and processes created by the federal government's investment in research and development. The Administration is vigorously implementing laws giving universities and small businesses ownership of technology developed with Federal funds.

The Administration is also reviewing, and will seek to amend where warranted, anti-trust laws or regulations that impede our international competitiveness.

INTERNATIONAL FINANCIAL AND DEVELOPMENT POLICIES

The Administration is also actively supporting U.S. trade interests by pursuing initiatives in the international financial and development policy area. At recent economic summit and ministerial meetings, we have urged our foreign partners to pursue economic growth-oriented policies. This would reduce the U.S. trade deficit through increased demand for our exports, and would also provide additional export opportunities for debt-ridden LDCs.

The Administration actively supports the efforts being coordinated by the International Monetary Fund and World Bank to help strengthen the international financial system and promote economic development.

To this end, the United States is prepared to consider the possible value of hosting a high-level meeting of the major industrial countries, to review the various issues involved in transforming the findings of the Group of Ten into appropriate action. Such a meeting could build on the G–10 studies by considering, in a cooperative fashion, the policies and performance in the major industrial countries, and how these can be improved to promote convergence toward noninflationary growth.

U.S. exports have suffered in recent years as a result of the external debt crisis affecting a number of developing countries. Conditional IMF financing programs can assist debtor countries in making a transition to sustainable growth. To this end, it is important that the United States support IMF efforts to seek macro and micro-economic policy reform as part of financial assistance packages negotiated with debtor countries.

The Administration believes that reform of trade and investment policies should be part of the policy reforms being negotiated by the IMF as part of conditional financing programs. Reduced export subsidies and liberalized trade barriers will benefit many developing countries' efforts to improve economic efficiency and accelerate economic growth. The Administration continues to press for these reforms in its representation and voting in the IMF. Such efforts will contribute to a more open and healthy international environment for U.S. and developing country trade and growth.

In its relations with the World Bank, the Administration has been pressing for expanding the role of the private sector in promoting long/term economic growth in developing countries. Administration support was instrumental in creating a $200 million private sector program affiliated with the Inter-American Development Bank.

The Administration believes that less government intervention in the economies of developing countries and fewer restrictions on domestic and foreign investment will greatly assist rapid development and growth of world trade. A liberalization of developing country restrictions on foreign investment can promote competition and reduce the inefficiency created by protected domestic monopolies, at the same time providing funds and productive capabilities to meet these countries' debt service requirements. The Administration supports the implementation of the Multilateral Investment Guarantee Agency recently negotiated in World Bank meetings, in order to help promote the international flow of investment. The Administration also encourages developing countries to stimulate investment by negotating agreements to protect and give national treatment to foreign investment, and by increasing the level of protection given to intellectual property.

The Administration will continue to press the World Bank to assist in promoting market-oriented development policies. Price controls and subsidies often distort both development and trade and lead to wasteful uses of World Bank funds and the development of industries whose survival in the international marketplace depends upon continuing government aids. Such policies can also inflict damage on U.S. industries which are in competition with government-assisted foreign companies. We have supported a number of loans by the multilateral development banks in support of market and trade reforms in developing countries.

TRADE POLICY: ENSURING BETTER ACCESS AND FAIRER TRADE

U.S. trade policy must be based on a realistic appraisal of the competitive position of the United States in the world economy. Clearly, our nation remains strong and vibrant, the economic leader of the free world with a political leadership role based on that strength. To carry out this role we must continue to devote our efforts in creating conditions of open and expanding international trade that will contribute to global prosperity.

The Administration reaffirms its basic trade policy position as enunciated in its July 8, 1981 statement. In accordance with that position, the Administration will continue to pursue more open access to markets abroad for U.S. exports and fairer conditions of trade, while opposing policies at home and abroad that are protectionist. We seek substantial trade liberalization from our major developed and advanced-developing country trade partners that will open more markets to U.S. products. The United States will take the initiatives necessary to achieve more equitable access in a number of foreign markets, particularly in Japan and major developing countries.

Our trade policy must combine concerted efforts with our trading partners to attain more open conditions in the world trading community over the long run with a willingness to take short-run steps, as necessary, to ensure fair competitive conditions for U.S. business firms.

Other nations must understand that the political support in the United States for maintaining and building a more open trading system will be impossible to maintain if progress in achieving more open and fair trade abroad is not made soon. The United States will always approach international trade issues in a determined, but non-confrontational, way. But, if necessary, we will take action to achieve more open foreign markets and defend ourselves against unfair foreign trade practices.

The Administration will step up the use of the authority given to it by Congress to address foreign unfair trade practices which distort U.S. trade and investment, and it will vigorously pursue U.S. trade interests and rights under U.S. laws and the GATT, and will see that other countries live up to their trade agreement obligations with the United States.

Further, we will continue to vigorously enforce U.S. laws aimed at countering foreign dumping and subsidy practices.

Competition in international trade should involve business firms, not government treasuries. The diligent negotiation of improved international rules on export subsidies, is a high-priority endeavor of this Administration. Where such rules are absent, inadequate, of unsatisfactory in their implementation the United States will vigorously defend its exporters against the subsidy programs of other nations.

The Administration will accelerate its efforts to address the problem of foreign governments' financial assistance to exports, particularly where mixed credits are involved, while pressing for international agreement to eliminate subsidized export financing. So-called "mixed credits" arises when governments combine export credits with financial assistance grants of funds in order to lower the cost of credit on their export sales. Mixed credits are a significant and growing subsidies problem in the world trading system. The Export-Import Bank will begin an aggressive, targeted mixed-credit lending policy. At the same time, the Administration will seek a $300 million appropriation for grants to support up to $1 billion in mixed-credit loans.

In the last two years, the Administration has successfully reached agreements to limit interest subsidies in export sales of large aircraft and nuclear power plants. These precedents in international cooperation must be extended to the mixed-credit problem as well.

The Administration will be receptive to petitions from U.S. firms and individuals that present valid companies about foreign unfair trade practices. The President recently announced that five cases would be initiated or accelerated under Section 301 of the Trade Act of 1974 to address unfair trade practices abroad. This is the first time that any President has taken this important step. The Administration will also take tactical measures aimed at eliminating unfair foreign trade practices and opening foreign markets, if efforts fail to resolve such issues through consultations. The denial or limitation of access to the U.S. market may be a necessary measure in this process.

The Administration supports the market-opening objectives of equitable access legislation but will oppose legislation that would require the President to close U.S. markets on the basis of sectoral reciprocity. The proper approach is to give the Administration authority to negotiate foreign barrier reductions. Further, the Administration will follow up on its report to the Congress on the subject of foreign industrial targeting by continuing to examine the potential problems created by foreign targeting and, where appropriate, possible remedies.

We will seek the removal of foreign barriers and distortions to U.S. trade in services and high technology industries (areas in which we have a significant worldwide competitive advantage) and to U.S. direct investment abroad. An important new trade priority will be to reduce and eliminate barriers to and distortions in U.S. trade arising from inadequate foreign protection of U.S.-generated intellectual property—patents, copyrights and trademarks.

In the agricultural trade area, the Administration will continue to counter foreign export subsidies which endanger our traditional overseas markets. The Administration will continue to explore possible uses of its export Payments-In-Kind (PIK) program to encourage our trade partners, particularly in Europe, to commit themselves to the elimination of agricultural export subsidies.

OCCASIONAL TEMPORARY SAFEGUARDS AND NATIONAL SECURITY

Free and fair trade is in the best interest of the citizens of the United States. Open trade produces more jobs, a more productive use of our nation's resources, more rapid innovation, and a higher standard of living. It also advances our national security interests by stengthening the economic and political systems of friendly nations. Protectionism, in the form of tariff surcharges or quotas, would be costly and contrary to our national economic and security interests.

It is, nevertheless, recognized internationally that nations may occasionally find it necessary to temporarily safeguard industries from serious harm caused primarily by a surge in imports. Occasional U.S. safeguard actions, taking accordance with our trade laws, are consistent with our international obligations. They must, however, reflect the nation's overall economic or security interests. Relief must be determined to be in the national economic interest; it must also be temporary, decline over the period of relief, and offer the prospect of adjustment on the part of the U.S. industry so that it will be competitive after the relief is terminated.

Instead of protection, the Administration will examine ways to promote worker retraining. The Administration will review existing worker assistance programs in order to assure that they promote an effective human adjustment policy which contributes to the maximum capacity for change, mobility, and increased productivity. This review will include an assessment of: (a) training and retraining programs—sponsored by government, labor and business—on a comprehensive and continuing basis; and (b) employment service, job bank, training, and relocation support for displaced workers in order to minimize human cost and the loss of valuable skills.

The Administration reserves the right to respond to economic conditions internationally and to levels of import penetration that threaten domestic industries essential to our long-term national security. Furthermore, the Administration will vigorously enforce our export control laws in the interest of our own national security. At the same time, the Administration recognizes the reality of foreign availability and the importance of our reputation as a reliable supplier. We are also aware that future technical advances by U.S. industry depend on maintaining the widest possible access to foreign markets and on fostering the widest exchange of scientific information.

INTERNATIONAL NEGOTIATIONS TO IMPROVE ACCESS AND ACHIEVE FAIRER TRADE

There is a great need to strengthen the international trading system through the cooperative efforts of the United States and its trade partners, in order to obtain better access and fairer conditions of international trade. There is a compelling need for overhaul of the General Agreement on Tariffs and Trade (GATT), which has provided the international legal framework for international trade over the past 40 years. The GATT's effectiveness has waned in recent years, primarily because its machinery and rules have not been adapted to current needs of the international trading community.

The GATT must be strenghened in the following areas: dispute settlement; discipline over import restraints (whether in the form of safeguards, and infant industry or balance of payments restrictions); and rules on the use of export subsidies. GATT negotiations must also achieve a vastly improved environment for the conduct of trade in agricultural products. Negotiations are needed to improve the non-tariff barrier codes which were initially developed in the Tokyo round. And the GATT must examine issues and extend its domain in areas which are increasingly important to international trade, including the protection of intellectual property, trade in services, and trade-distorting investment practices.

The United States has urged its trade partners to enter into a new multilateral negotiating round soon to deal with these issues in the GATT. Such a round would send a positive signal that GATT members reaffirm their belief in an open trading system and in the GATT as an institution capable of adapting itself to changing conditions. These negotiations should begin in early 1986.

While our highest priority remains the improvement of the world trading system through a new round of multilateral trade negotiations, the United States is interested in the possibility of achieving further liberalization of trade and investment through the negotiation of bilateral free-trade arrangements such as the one recently concluded with Israel. We believe that, at times, such agreements could complement our multilateral efforts and facilitate a higher degree of liberalization, mutually beneficial to both parties, than would be possible within the multilateral context.

The United States will give careful consideration to any serious proposal to enter into the negotiation of such agreements. The paramount factor in evaluating such proposals will be their economic value to the United States; we will not pursue any agreement which is not clearly in our economic and commercial interest. Finally, the prospects for significant progress in a new round of multilateral trade negotiations will also influence our deliberations on such bilateral initiatives.

The Administration will consult closely with Congress and with representatives of the private sector before entering into formal negotiations aimed at reaching any bilateral free-trade arrangements and it will also notify Congress of its intentions in accordance with existing U.S. law.

In addition to possible bilateral free-trade arrangements, the United States will undertake other bilateral efforts to improve access for U.S. trade and investment. These bilateral efforts could address specific or sectoral trade issues. Recently, the United States entered into sector-specific discussions with the government of Japan to improve access for U.S. producers of telecommunications equipment, medical and pharmaceutical products, electronics goods and forestry products. New sectors will be added that offer the promise of expanded U.S. exports.

The Administration also entered into discussions with the Japanese government to seek more open financial markets in Japan and a role for the yen which more closely reflects Japan's increasing economic importance in the world economy. We will be following-up on the implementation of commitments made by Japan in this area.

Other bilateral initiatives include market-opening discussions with advanced developing countries (for example, Taiwan and Korea) and initiatives to negotiate bilateral investment treaties with developing countries. Such treaties provide nondiscriminatory treatment, protection against expropriation, the right of free transfer of funds, the arbitration of investment disputes and the coverage of intellectual property of U.S. investors.

SUMMARY OF THE ADMINISTRATION'S TRADE POLICY

At this time of major challenge to the future of U.S. and world trade, the Administration will carry out an active program to address the key elements of its trade strategy—maintenance of a strong and growing domestic and international economy and more open and fair conditions for U.S. trade. In summary the Administration will do the following:

DOMESTIC AND INTERNATIONAL ECONOMIC POLICIES

1. The Administration will, for the benefit of our international trade as well as our overall domestic economy, vigorously seek to bring federal spending under control. The Congress and public must clearly recognize the adverse impact of excessive government spending and budget deficits on the dollar's value and U.S. trade. As Congress wishes to contribute to reducing the trade deficit, it should focus its energies on cutting excessive spending and budget deficits rather than supporting protectionist legislation.
2. The Administration will, continue to press for the adoption of the President's tax reform proposal, which is essential to strengthening our economy and making U.S. businesses more competitive in international markets.
3. The Administration will review, and will seek to amend if warranted, our domestic anti-trust laws or regulations to the extent that they impede our international competitiveness.
4. The Administration will consider trade implications when reviewing proposed regulations and when developing further deregulation initiatives. The Administration will use the leverage created by its deregulatory process to seek to open foreign markets, thereby minimizing the problem of free rides for foreign suppliers.
5. The Administration will increase efforts to protect intellectual property rights (patents, copyrighjts, trademarks); we will accelerate work in this area with a view toward possible Administration legislative and administrative initiatives.
6. The U.S. will encourage our trading partners to adopt policies that will accelerate their economic growth, thereby expanding our export opportunities. Specifically we will urge Bonn Summit participants to act on their commitments to remove rigidities and imbalances in their economies. The U.S. will also continue to use discussions in the IMF and OECD to pursue this strategy.
7. The Administration will encourage debtburdened LDCs to reduce government impediments to the functioning of markets in their economies, encourage production through market incentives to their business firms and employees, and substitute equity capital for debt by encouraging both domestic and foreign investment.
8. The 1984 yen-dollar efforts toward liberalizing Japan's financial markets and internationalizing the yen will continue.

FREE AND FAIR TRADE POLICIES

9. Because the the Administration depends upon both exports and imports for its prosperity and because protectionism is costly and counterproductive, the Administration's goal will be to work toward a more free and fair trading system.
10. The United States will vigorously pursue its rights and interests in international commerce under U.S. law and the GATT, and will see that other countries live up to their obligations and trade agreements with the United States.
11. The Administration will continue vigorous enforcement of U.S. antidumping and countervailing duty laws.
12. In the past, the United States has initiated Section 301 unfair trade investigations only in response to formal petitions for action from U.S. industries. The Administration will, as appropriate, also self-initiate such cases to address foreign unfair trade practices.
13. Where export subsidy rules are absent, inadequate, or unsatisfactory in their implementation, the U.S. will vigorously defend its exporters against the subsidy progress of other nations. Also, the Export-Import Bank will begin an aggressive targeted mixed-credit lending policy. At the same time, the Administration will seek a $300 million appropriation for grants to support up to $1 billion in mixed-credit loans.
14. The Administration will take tactical measures aimed at eliminating unfair foreign trade practices and opening foreign markets, if efforts to resolve such issues

through consultations fail. The denial or limitation of access to the U.S. market may be a necessary measure in this process.

15. The Administration will support the market-opening objectives of equitable access legislation; but it will oppose legislation that would require the President to close U.S. markets on the basis of sectoral reciprocity. The proper approach is to grant the Administration authority to negotiate foreign barrier reductions.

16. The United States will continue market-oriented sector selective (MOSS) discussions with Japan. However, time limits will be placed on existing sector discussions, at the end of which specific commitments will be evaluated and follow-up procedures begun. New sectors will be added that offer the promise of expanded U.S. exports.

17. The Administration will follow up on its reports to the Congress on the subject of foreign industrial targeting by continuing to examine the potential problems created by foreign targeting and, where appropriate, possible remedies:

U.S. EXPORT PROMOTION POLICIES

18. The United States will seek to reduce our nation's trade deficit through increasing exports instead of restricting imports.

19. The Administration will work with private sector advisory groups (e.g., the President's Export Council) to improve export promotion and to help U.S. companies expand their global marketing efforts.

20. The Administration will evaluate Federal export promotion activities during the fall budget review, and alter these activities as necessary to improve their effectiveness.

21. The Administration will again seek legislation to remove the export disincentives in the Foreign Corrupt Practices Act.

MULTILATERAL AND BILATERAL TRADE NEGOTIATIONS FOR U.S. EXPORTS AND FAIR TRADE

22. There is a great need for a more comprehensive disciplined and effective system of world trade rules. The Administration will maintain efforts to launch a new GATT trade round.

23. The Administration will examine possible bilateral and plurilateral negotiating opportunities, both to improve market access and enhance fairness and promote wider interest in the multilateral negotiating process.

SAFEGUARDS AND NATIONAL SECURITY POLICIES

24. The Administration is committed to market-based solutions to trade problems, at home and abroad; but occasional exceptions may be necessary.

25. Import relief, when undertaken, will be transparent, temporary, time-specific, and will decline over the period of relief, and lead to international competitiveness.

26. The Administration will review existing worker assistance programs in order to assure that they promote an effective human adjustment policy.

27. The Administration reserves the right to respond to economic conditions internationally and to levels of import penetration that threaten domestic industries essential to our long-term national security.

28. The Administration will vigorously enforce our export control laws in the interest of our own national security. At the same time, the Administration recognizes the reality of foreign availability and the importance of our reputation as a reliable supplier.

The President's Trade Policy Action Plan

Fact Sheet

The President's trade policy is based on five principles:

1. Free trade and fair trade are in the best interest of the citizens of the United States. Free trade produces more jobs, a more productive use of our nation's resources, more rapid innovation, and a higher standard of living. Free trade also advances our national security interests by strengthening the economic and political systems of our allies. Fair trade based upon mutually acceptable rules is necessary for support of free trade.

2. The United States plays the critical role in ensuring and promoting an open trading system. If the United States falters in its defense and promotion of the free worldwide trading system, the system will collapse, adversely affecting our national well-being.

3. The United States' role does not absolve our trading partners of a major obligation to support a more open trading system. This obligation includes: dismantling trade barriers, eliminating subsidies and other forms of unfair trade practices, and entering into trade liberalization negotiations in the GATT.

4. The international trading system is based upon cooperation. Since World War II, we have made significant progress in moving toward an open worldwide trading system. Protectionism threatens to undermine the system. Our trading partners must join us in working to improve the system of trade that has contributed to economic growth and security of ourselves and our allies.

5. America has never been afraid to compete. When trade follows the rules, and there is an equal opportunity to compete, American business is as competitive as any. This is fair trade and we will not impair it. When these conditions do not exist, it is unfair trade, and we will fight it.

The President has taken a number of actions to translate these principles into policy.

MAKING FREE TRADE FAIR TRADE

The President will vigorously pursue U.S. rights and interests in international commerce under U.S. law and the GATT, and will see that other countries live up to their obligations and trade agreements with the U.S. More specifically:

1. The President will attack foreign unfair trade practices. The President has directed the United States Trade Representative to initiate or accelerate unfair trade practices proceedings, the first time done so by a President of the United States. Other actions, when appropriate, will be taken. Proceedings accelerated or initiated so far are:

Japanese leather and leather footwear import restrictions;
European Community canned fruit subsidies;
Korean insurance policy barriers;
Brazil's import restrictions on micro-electronics products; and
Japanese tobacco restrictions.

2. To discourage our trading partners from seeking unfair advantage by using predatory credits to subsidize their exports, the President will propose that Congress approve a fund of $300 million in grants which would support up to $1 billion in tied-aid credits to maintain U.S. markets in the face of this practice.

3. The President has directed the United States Trade Representative to initiate and accelerate both bilateral and multilateral negotiations with countries where the counterfeiting or piracy of U.S. goods has occurred. The Administration will increase efforts to protect intellectual property rights (patients, copyrights, trademarks), with a view toward possible legislative or administrative initiatives.

4. The President has directed that a strike force be established among the relevant agencies of the Federal Government, with the task of identifying unfair foreign trade practices and executing the actions necessary to counter and eliminate the unfair practices.

5. The President has directed the Secretary of State to seek time limits on the current discussions with Japan designed to open access to specific Japanese markets, at the end of which specific commitments will be evaluated and follow-up procedures begun. New sectors will be added that offer the promise of expanded U.S. exports.

PROMOTING FREE TRADE AND EXPORTS

The United States is a great trading nation. The health of our economy depends on both exports and imports. The President's goal is to preserve as free and open a trading system as possible. A free and open system will be a fair system.

1. The President seeks to engage our trading partners in multilateral negotiations in the GATT to achieve freer trade, increase access for U.S. exports, provide more effective dispute resolution, and strengthen the fabric of the international trading system.

The President wants to use the multilateral negotiating process to eliminate unfair trade practices and improve access for U.S. exports, particularly agriculture and high technology, and address newer forms of international trade problems, including interlectual property protection, services trade, and investment issues.

2. The President will also explore possible bilateral and regional trade agreements that would promote more open trade and serve U.S. economic interests.

3. The President has directed the Secretary of Commerce and the Economic Policy Council, in conjunction with the President's Export Council, to review current export promotion activities with a view toward strengthening them and increasing

private sector involvement. The Commerce Department will also work with state governments interested in expanding their export promoting activities.

4. To better assist workers in adjusting to the dynamics of the world trading system, the President has directed the Secretary of Labor and the Economic Policy Council to review existing worker assistance programs to assure that they promote an effective policy that contributes to maximum capacity for change, mobility, and increased productivity.

IMPROVING THE WORLD AND DOMESTIC ECONOMIC ENVIRONMENTS

The trade deficit has grown because economic difficulties abroad have persisted while the U.S. has been more successful in utilizing our economic opportunities. Better balance in world economic performance must be achieved.

1. To do our share in achieving the needed balance in the world economy and lowering the value of the dollar, the United States must reduce excessive government spending. The President will hold Congress to no more than the spending levels established in the Senate budget resolution.*

2. The President will press for his tax reform proposal, which is essential to strengthening the economy and making U.S. businesses more competitive in international markets.

3. The President has directed the Economic and Domestic Policy Councils to review, and if warranted, seek to amend antitrust laws that impede our international competitiveness. The President will also use the trade leverage created by domestic deregulation to seek to open foreign markets.

4. The President authorized the Secretary of the Treasury to join his counterparts from other major industrial countries yesterday to announce measures to promote stronger and more balanced growth in our economies and the strengthening of foreign currencies. This will provide better markets for U.S. producers and improve America's competitive position.

5. The United States is prepared to consider the value of hosting a high-level meeting of the major industrial countries to review, implement and build upon the Group of Ten monetary studies by considering in a cooperative fashion, the policies and performance of the major industrial countries, and how these can be improved to promote convergence toward non-inflationary growth.

6. The President has also directed the Secretary of the Treasury to use the international financial institutions to encourage debt-burdened LDCs to reduce government impediments to the functioning of markets, encourage private sector production, and substitute equity capital for debt by encouraging both domestic and foreign investment.

LEGISLATION WHICH WOULD REFLECT THE PRESIDENT'S PRINCIPLES AND POLICIES WOULD ENCLUDE

1. Trade negotiating authority

Authority to support trade negotiating initiatives including:

A new round of negotiations;

Elimination of non-tariff barriers (current authority expires January 3, 1988);

Tariff reductions; and

Compensation to other countries when the U.S. increases tariffs (through Congressional action or customs reclassification) to avoid unilateral foreign retaliation against U.S. exports.

2. Intellectual property rights

Further protection of intellectual property rights (patents, copyrights or trademarks), including:

Protecting against trade is articles that infringe U.S. process patents;

Extending the patent term for agricultural chemicals to match that for pharmaceutical inventions;

Eliminating the requirement in Section 337 of injury to as efficiently and economically operated U.S. industry as a procondition for a relief where the International Trade Commission found a patent, trademark or copyright infringement;

More liberal licensing of technology under the antitrust laws;

Better protecting "firmware through amendments to U.S. copyright law; and

---

*Addendum: The President will hold Congress to the House/Senate Budget Resolution.

Eliminating Freedom of Information Act abuses by giving affected companies notice and an opportunity to oppose release of their business confidential information.

3. Export promotion

Promote U.S. exports through:

Submitting legislation authorizing and appropriating approximately $300 million in grant funds to enable the Administration to offer $1 billion in mixed credit loans to targeted buyers. This program is designed to enable U.S. exports to compete effectively in third country markets until we can eliminate predatory mixed credit competition through negotiations;

Clarifying the accounting provisions and liabilities at foreign agents under the Foreign Corrupt Practices Act of 1977 to reduce disincentives to export;

Allowing U.S. companies to export new drugs and biologicals not yeat approved by the Food and Drug Administrator to countries where they can be sold lawfully.

4. Existing trade laws

Strengthen the antidumping and countervailing duty laws with a predictable pricing test for non-market economies, place deadlines on Section 301 dispute settlement, and establish section 201 fast track procedure for perishable items.

ANNOUNCEMENT OF THE MINISTERS OF FINANCE AND CENTRAL BANK GOVERNORS OF FRANCE, GERMANY, JAPAN, THE UNITED KINGDOM, AND THE UNITED STATES

1. Ministers of Finance and Central Bank Governors of France, the Federal Republic of Germany, Japan, the United Kingdom, and the United States met today, September 22, 1985, in the context of their agreement to conduct mutual surveillance and as part of their preparations for wider international discussions at the forthcoming meetings to Seoul, Korea. They reviewed economic developments and policies in each of their countries and assessed their implications for economic prospects, external balances, and exchange rates.

2. At the Bonn Economic Summit in May 1985 the Heads of State or Government of seven major industrial countries and the President of the Commission of the European Communities issued an Economic Declaration Toward Sustained Growth and Higher Employment. In that Declaration the participants agreed that: "The best contribution we can make to a lasting new prosperity in which all nations can share is unremittingly to pursue, individually in our own countries and cooperatively together, policies conductive to sustained growth and higher employment."

3. The Ministers and Governors were of the view that significant progress has been made in their efforts to promote a convergence of favorable economic performance among their countries on a path of steady noninflationary growth. Furthermore, they concluded that their countries are restoring the vitality and responsiveness of their economies. As a result of these developments, they are confident that a firm basis has been establish for a sustained, more balanced expansion among their countries. This sustained growth will benefit other industrial countries and will help ensure expanding export markets for developing countries, thereby contributing importantly to the resolution of problems of heavily indebted developing countries.

4. They believe that this convergence of favorable economic performance has been influenced increasingly by policy initiatives undertaken by their countries. Moreover, each of their countries is committed to the implementation of further policy measures which will reinforce favorable convergence and strengthen the sustainability of the current expansion.

5. Ministers and Governors were of the view that recent shifts in fundamental economic conditions among their countries, together with policy commitments for the future, have not been reflected fully in exchange markets.

RECENT ECONOMIC DEVELOPMENTS AND POLICY CHANGES

6. Ministers and Governors expect that real growth in aggregate for their countries will be about 3 percent this year, compared to negative growth of −0.7 percent in 1982. Although this figure is down slightly from 1984, growth will be more balanced than at any time in the last four years. After the particularly rapid U.S. growth of 1983–84, there is now increased evidence of internal growth in the other countries. In particular, private investment has picked up strength. The current expansion is occurring in a context of fiscal consolidation; it is not dependent on short-lived fiscal stimulus. As a result of the changes in the components of growth, real

growth in their countries can be expected to remain strong as U.S. growth moderates.

7. The current sustained expansion is occurring within a framework of declining inflation, a phenomenon that is unprecedented in the past three decades. Inflation rates are at their lowest in nearly 20 years, and they show no signs of reviving.

8. There has been a significant fall in interest rates in recent years. Apart from welcome domestic effects, this has been particularly helpful in easing the burden of debt repayments for developing countries.

9. This successful performance is the direct result of the importance given to macroeconomic policies which have reduced inflation and inflationary expectations, to continued vigilance over government spending, to greater emphasis on market forces and competition, and to prudent monetary policies.

10. These positive economic developments notwithstanding, there are large imbalances in external positions which pose potential problems, and which reflect a wide range of factors. Among these are: the deterioration in its external position which the U.S. experienced from its period of very rapid relative growth; the particularly large impact on the U.S. current account of the economic difficulties and the adjustment efforts of some major developing countries; the difficulty of trade access in some markets; and the appreciation of the U.S. dollar. The interaction of these factors—relative growth rates, the debt problems of developing countries, and exchange rate developments—has contributed to large, potentially destabilizing external imblances among major industrial countries. In particular, the United States has a large and growing current account deficit, and Japan, and to a lesser extent Germany, large and growing current account surpluses.

11. The U.S. current account deficit, together with other factors, is now contributing to protectionist pressures which, if not resisted, could lead to mutually destructive retaliation with verious dmage to the world economy; world trade would shrink, real growth rates could even turn nagative, unemployment would rise still higher, and debt-burdened developing countries would be unable to secure the export earnings they vitally need.

POLICY INTENTIONS

12. The Finance Ministers and Governors affirmed that each of their countries remains firmly committed to its international responsibilities and obligations as leading industrial nations. They also share special responsibilities to ensure the mutual consistency of their individual policies. The Ministers agreed that establishing more widely strong, noninflationary domestic growth and open markets will be a key factor in ensuring that the current expansion continues in a more balanced fashion, and they committed themselves to policies toward that end. In countries where the budget deficit is too high, further measures to reduce the deficit substantially are urgently required.

13. Ministers and Governors agreed that it was essential that protectionist pressures be resisted.

14. Ministers recognized the importance of providing access to their markets for LDC exports as those countries continue their essential adjustment efforts, and saw this as an important additional reason to avoid protectionist policies. They welcomed the GATT preparatory meeting scheduled for late September and expressed their hope that it will reach a broad consensus on subject matter and modalities for a new GATT round.

15. In this context, they recalled and reaffirmed the statement in the Bonn Economic Declaration on the debt situation.

Sustained growth in world trade, lower interest rates, open markets and continued financing in amounts and on terms appropriate to each individual case are essential to enable developing countries to achieve sound growth and overcome their economic and financial difficulties.

16. The Ministers agreed that they would monitor progress in achieving a sustained noninflationary expansion and intensify their individual and cooperative efforts to accomplish this objective. To that end, they affirmed the statements of policy intentions by each of their countries. which are attached.

CONCLUSIONS

17. The Ministers of Finance and Central Bank Governors agreed that recent economic developments and policy changes, when combined with the specific policy intentions described in the attached statements, provide a sound basis for continued and a more balanced expansion with low inflation. They agreed on the importance of these improvements for redressing the large and growing external imbalances

that have developed. In that connection, they noted that further market-opening measures will be important to resisting protectionism.

18. The Ministers and Governors agreed that exchange rates should play a role in adjusting external inbalances. In order to do this, exchange rates should better reflect fundamental economic conditions than has been the case. They believe that agreed policy actions must be implemented and reinforced to improve the fundamentals further, and that in view of the present and prospective changes in fundamentals, some further orderly appreciation of the main non-dollar currencies against the dollar is desirable. They stand ready to cooperate more closely to encourage this when to do so would be helpful.

The *French Government* intends to pursue its policy aimed at reducing inflation, moderating income growth, and achieving continued improvements in external accounts. It will further intensify its efforts to speed up structural adjustment and modernization and thus lay the basis for job creating growth.

Therefore, it is determined:

1. To pursue vigorously disinflation.
2. To secure the attainment of monetary aggregates growth targets, consistent with decelerating inflation.
3. To curb public expenditures progressively so as to lower the tax burden while reducing the government borrowing requirement.
4. To foster the investment recovery allowed for by the improved financial situation in the business sector.
5. To take further steps toward liberalization and modernization of financial markets, to increase competition in the financial sector so as to reduce financial intermediation costs and give a greater role to interest rates in monetary control.
6. To foster job creation through the implementation of an innovative and active policy in the field of education and training and by promoting constructive discussions between social partners on work organization.
7. To resist protectionism.

The *Government of the Federal Republic of Germany,* noting that the German economy is already embarked on a course of steady economic recovery based increasingly on internally generated growth, will continue to implement policies to sustain and extend the progress achieved in strengthening the underlying conditions for continuing, vigorous, job-creating growth in the context of stable prices and low interest rates.

In particular, the Government of the Federal Republic of Germany will implement policies with the following explicit intentions.

1. The priority objective of fiscal policy is to encourage private initiative and productive investments and maintain price stability.
2. Toward this end, the Federal Government will continue to reduce progressively the share of the public sector in the economy through maintaining firm expenditure control. The tax cuts due to take effect in 1986 and 1988 form part of the ongoing process of tax reform and reduction which the Federal Government will continue in a medium-term framework.
3. The Federal Government will continue to remove rigidities inhibiting the efficient functioning of markets. It will keep under review policies, regulations, and practices affecting labor markets in order to enhance the positive impact of economic growth on employment. The Federal Government and the Deutshe Bundesbank will provide the framework for the continuing evolution of deep, efficient money and capital markets.
4. The fiscal policy of the Federal Government and the monetary policy of the Deutsche Bundesbank will continue to ensure a stable environment conducive to the expansion of domestic demand on a durable basis.
5. The Federal Government will continue to resist protectionism.

The *Government of Japan,* noting that the Japanese economy is in an autonomous expansion phase mainly supported by domestic private demand increase, will continue to institute policies intended to ensure sustainable noninflationary growth; provide full access to domestic markets for foreign goods, and internationalize the yen and liberalize domestic capital markets.

In particular, the Government of Japan will implement policies with the following explict intentions.

1. Resistance of protectionsim and steady implementation of the Action Program announced on July 30 for the further opening up of Japan's domestic market to foreign goods and services.
2. Full utilization of private sector vitality through the implementation of vigorous deregulation measures.
3. Flexible management of monetary policy with due attention to the yen rate.

4. Intensified implemention of financial market liberalization and internationalization of the yen, so that the yen fully reflects the underlying strength of the Japanese economy.

5. Fiscal policy will continue to focus on the twin goals of reducing the central government deficit and providing a pre-growth environment for the private sector. Within that framework, local governments may be favorably allowed to make additional investments in the FY 1985, taking into account the individual circumstances of the region.

6. Efforts to stimulate domestic demand will focus on increasing private consumption and investment through measures to enlarge consumer and mortgage credit markets.

The *United Kingdom Government*, noting that the British economy has been experiencing steady growth of output and domestic demand over the past four years, will continue to pursue policies designed to reduce inflation, to promote sustained growth of output and employment; to reduce the size of the public sector; to encourage a more competitive, innovative, market orientated private sector; to reduce regulation and increase incentives throughout the economy; and to maintain open trading and capital markets free of foreign exchange controls.

In particular, the United Kingdom Government intends:

1. To operate monetary policy to achieve further progress towards price stability and to provide a financial environment for growing output and employment; and to buttress monetary policy with a prudent fiscal policy.

2. To continue to reduce public expenditure as a share of GDP and to transfer further substantial parts of public sector industry to private ownership.

3. To reduce the burden of taxation in order to improve incentives and to increase the efficient use of resources in the economy.

4. To take additional measures to improve the effective working of the labour market, including the reform of Wages Counciles and improvements in youth training; and implement proposals to liberalize and strengthen competition within financial markets.

5. To resist protectionism.

The *United States Government* is firmly committed to policies designed to: ensure steady noninflationary growth; maximize the role of markets and private sector participation in the economy; reduce the size and role of the government sector; and maintain open markets.

In order to achieve these objectives, the United States Govenrment will:

1. Continue efforts to reduce government expenditures as a share of GNP in order to reduce the fiscal deficit and to free up resources for the private sector.

2. Implement fully the deficit reduction package for fiscal year 1986. This package passed by Congress and approved by the President will not only reduce by over 1 percent of GNP the budget deficit for FY 1986, but lay the basis for further significant reductions in the deficit in subsequent years.

3. Implement revenue-neutral tax reform which will encourage savings, create new work incentives, and increase the efficiency of the economy, thereby fostering noninflationary growth.

4. Conduct monetary policy to provide a financial environment conducive to sustainable growth and continued progress toward price stability.

5. Resist protectionist measures.

The CHAIRMAN. Mr. Ambassador, thank you. We will question you on a first-come, first-served basis; and the order I have is Senators Baucus, Moynihan, Packwood, Wallop, Chafee, and Long, and now Grassley.

Senator BAUCUS. Thank you very much, Clayton. I wonder if we could talk a little about the new GATT round: What should be included and what should not, what objections you expect us to run up against as we try to formulate what should be discussed and not discussed. I want to give you that open ended question. Could you for just a few minutes tell us what you think should be included: What services, what kinds of services? Should we address the wage rates, for example? Is that an unfair trading practice, or might it be an unfair trading practice? Health standards, safety standards, or the lack thereof, here and in other countries? We can agree at least that that is a Government policy that affects trade. What should be included and what should not, and what do you think we will be up against?

Ambassador YEUTTER. Thank you, Senator Baucus. I appreciate the chance to respond to that question because I really believe it is an extremely important issue for the United States right now.

I must preface my comments by saying that I am much more convinced today than I was 4½ months ago of the importance to the United States of moving into a new GATT round. I am really strongly convinced that we need to get there, and get there as quickly as possible. We just have a lot of things that need to get done.

Let me articulate a few of those, and I will do them very quickly. In new areas—and this is where most of the contentiousness arises with our LDC trading partners—it is important that we get GATT rules developed, in my judgment, in at least three areas. I might add more to this list, but I will list the three that I believe are extremely high priority; and those are services, intellectual property, and investment. Services, because that is over 50 percent of our GNP today; and we have interests in insurance and banking and data processing and telecommunications and communications.

In a broader sense, shipping, transportation, tourism, media activities, and one can go on and on. There is essentially nothing in the way of international rules in these areas, and we have a lot at stake. Many of these areas, Senator Baucus, are areas in which we have a clear competitive advantage in the United States. The whole services area is one of those.

The second area is investment; and in my judgment, the attitude of the lesser developed countries on this issue is simply incongruous. If anybody in the world needs more investment, it is the LDC's. Ghana, for instance, can't get enough developed from their own resources. They need to attract capital from abroad.

Senator BAUCUS. Aren't some countries resisting that investment though?

Ambassador YEUTTER. Absolutely, and it is foolish to do so.

Senator BAUCUS. Why is that?

Ambassador YEUTTER. This is a classic example, Senator Baucus, of shooting oneself in the foot, with policies that make no sense at all. Those nations must develop an attractive investment environment if people from the United States or any other developed countries are going to make significant commitments into those economies. Right now, though, they are not attractive, that is the investment opportunities are not attractive; and that has to change.

Senator BAUCUS. Is that based on some sense of nationalism? Why are some countries resisting?

Ambassador YEUTTER. A lot of it is nationalistic: The fear that they will be taken over, if you will. They fear that their economies will be taken over and controlled by foreigners. In my judgment, that is an irrational fear, but I suppose not a surprising one. It is one that has prevailed for a long time, but it is so foolish because those nations are relegating themselves to inordinately low standards of living forevermore, unless they alter their course. It is just so important that we have investment rules, and it is more important for them than it is for us; but it is important for us, too, as investors.

Senator BAUCUS. What about the comparative wage rates?

Ambassador YEUTTER. On comparative wage rates, Senator——

Senator BAUCUS. I asked that because on the textile bill last night, Senator Packwood and I and others asked the ITC to do a study of comparative wage rates.

Ambassador YEUTTER. I certainly would have no objection to the ITC conducting a study because knowledge in that area will be helpful; but I really do not believe that it should be our prerogative to dictate to another nation what its wage rates shall be.

Senator BAUCUS. What if wage rates are subsidized?

Ambassador YEATTER. In my judgment, if wage rates are subsidized in some manner, that could certainly be construed as an "unfair trade practice," as I would define that term. Now, whether we can identify the subsidies that might be involved, I——

Senator BAUCUS. I am sorry. You mentioned a third area that you thought should be included in the GATT round?

Ambassador YEUTTER. Yes. The other one in the new areas would be intellectual property, and this is trademarks, copyrights, and patents, which is an area, Senator Baucus, where we are being subjected to international piracy. We are losing billions of dollars of export sales because of the inadequacy of rules on intellectual property. So, that is as far as we can go in the new areas. There is a lot of work, too, Senator Baucus, that needs to be done on the nontariff measure codes that were first enacted in the Tokyo round but which are badly in need of perfecting or of polishing. And let me add just one final point. Probably the most important objective of all in a new GATT round should be dispute settlement: The grossly inadequate dispute settlement mechanism that exists today.

Senator BAUCUS. I agree with you. Thank you very much.

The CHAIRMAN. Senator Moynihan?

Senator MOYNIHAN. Mr. Ambassador, you said something just a moment ago, or you were on the verge of saying something that seemed to me to be extraordinarily important. I wonder if you could expand on that. You seemed to suggest that the GATT arrangement may be breaking down and that the United States may have to consider a new regime in international trade all together. That was not a casual remark. Do you want to tell us what is happening in Geneva? Which groups are vetoing the proposal for a new round? I mean, speak. [Laughter.]

Ambassador YEUTTER. You did hear me correctly, Senator Moynihan, and that was certainly not a cavalier remark. It is an expression of deep concern with respect to what is transpiring in Geneva or what has been transpiring in the past couple of weeks. In my judgment, the GATT is in jeopardy. Even the Secretary-General, Mr. Dunkle, is expressing concern now with the conduct of some of the GATT members.

Senator MOYNIHAN. But what is happening? Are there people who are saying they don't want the new round?

Ambassador YEUTTER. Basically, what they are saying, Senator Moynihan, is that they do not want to discuss these issues that we deem to be important to the United States; or, alternatively, if we do discuss them, they would like them in a separate exercise, if you will. Or putting it another way: They would like to have their cake and eat it, too. They would like for us to make concessions in a negotiation on goods that would give them additional access into the U.S. market with little or no compensation on their part in terms of access to their markets. In other words, they would like a continuation of the special differential treatment of goods.

Senator **MOYNIHAN**. I guess we need some names. You mentioned the nations that account for 5 percent of world GNP. Do you mean the LDC's?

Ambassador **YEUTTER**. Yes. It is not all of the LDC's, however; it would be unfair to earmark all of them in that category. This effort is being led by Brazil and India, and they have been joined by—and I will let my people behind me give me the names if I don't catch them all—primarily Yugoslavia, Egypt, Nigeria, Argentina sometimes, and one or two others.

Senator **MOYNIHAN**. All right. Listen, maybe we can help you on that. I was once Ambassador to India, and I watched them just close out foreign investments all together and do it as a kind of political decision—a civil service kind of decision—which has clearly not been to their advantage. Those middle countries, which have great potential—what is that line of one of our Nobel laureate economists? He spoke of the miracle of nongrowth in Argentina; that was Paul Samuelson. If we can help you there, that is this committee—and I can't speak, of course, for the committee—those are good friends and they should be good trading partners; and that kind of behavior could bring the whole system crashing down.

Ambassador **YEUTTER**. It certainly could, Senator Moynihan. As I said earlier, we just cannot permit that kind of rigidity and intransigence to paralyze the GATT. We don't want to have a situation like the one you faced in the United Nations.

Senator **MOYNIHAN**. You said Brazil, Argentina, Yugoslavia. You have about a quarter of the world's population there and a great deal of its potential economic growth.

Ambassador **YEUTTER**. That is right.

Senator **MOYNIHAN**. India has the third largest work force of engineers and technologists in the world. There is a France inside India, just waiting to open.

Ambassador **YEUTTER**. And what is so paradoxical about that, Senator Moynihan, is that it seems to me that a new GATT round is as much or more in their interest as it is in the interest of anybody in the world. And I have told them that they should be the demondeurs in this process, and yet they are engaging in a resistance effort.

Senator **MOYNIHAN**. My time is up, but can we hear more from you on how we can help you? If the GATT system goes crashing down over something like this, then we have more than a problem of protectionism. We have a problem of trade barriers, and we have a problem of a trading system collapsing.

Ambassador **YEUTTER**. Precisely. We will appreciate the help, and the next 2 weeks or so will be critical in that regard.

Senator **MOYNIHAN**. And could I say that in the next 2 weeks or so this committee would very much appreciate the help from the administration with respect to the legislation we have adopted on trade adjustment assistance? It is not easy for you to come up here; but we passed unanimously in this committee an important provision on trade adjustment which has always accompanied the new

GATT rounds. And what do we hear from Mr. Miller and Mr. Regan? We hear that if the trade adjustment assistance provisions remain in the reconciliation bill, the President will veto it. Now, that is not the way to get along. [Laughter.]

Ambassador YEUTTER. Senator Moynihan, I will communicate your views personally.

Senator MOYNIHAN. Thank you, sir.

The CHAIRMAN. Mr. Ambassador, I have some questions from Senator Wallop that I will give you to answer in writing.

Ambassador YEUTTER. All right.

The CHAIRMAN. In response to Senator Baucus' question about wage differentials, you responded that that should not be an unfair trade practice per se.

Ambassador YEUTTER. Correct. In my judgment, there is no doubt that we are at a disadvantage in wage rates, vis-a-vis many other countries. Now, that is obvious in Asia in particular where wage rates in Korea, Taiwan, China, and a number of other countries are substantially below ours; and yet those countries also are rapid adapters of new technology and they have excellent management skills, which is why they are enormously productive and competitive these days.

The CHAIRMAN. Let me follow up then. They have all of the advantages of machines as modern as ours. They have a tremendous wage differential. Does that mean that for some industries in this country they cannot compete in this market against products from those countries, principally because of the wage differential?

Ambassador YEUTTER. In some, Senator Packwood, that is correct. In my judgment, not a lot of industries and even within industries, obviously some firms will be competitive with their counterparts in Asia and some will not.

The CHAIRMAN. Why?

Ambassador YEUTTER. Because some firms are better managed than others. Some firms take advantage of economies of scale and other economic attributes, and others do not. Some have better marketing programs, better brand names, more attractive brand names, and so on. So, there are a lot of factors that go into the definition of competitiveness.

The CHAIRMAN. What are some of those industries in the United States that just cannot compete solely on the wage differential?

Ambassador YEUTTER. By and large, as you well know, Senator Packwood, it would be labor-intensive industries, and they will be most of the industries that have had discussions with you and with us in recent weeks and months—textiles, footwear, and then some other labor-intensive industries of that ilk—coupled with other industries in, for example, steel, copper, and so on, where wage rates have typically been very high, that are not labor-intensive, even below-wage-rate industries, if one can define them as that, as well as the high-wage-rate industries where wages have gotten out ahead of productivity.

The CHAIRMAN. And these are industries that cannot compete against foreign competition because of the wage differential in this market?

Ambassador YEUTTER. It is difficult to aggregate and to generalize, but yes.

The CHAIRMAN. Yes. I realize that there are some exceptions. As a matter of fact, at one of our future hearings, we are going to have a steel company testify that indeed they can compete, but I am talking generally.

Ambassador YEUTTER. Yes, sir.

The CHAIRMAN. Now, if they cannot compete in this market, and that is going to be a permanent problem for them because of the wage differentials, should our policy be to protect them or should our policy be to let them go?

Ambassador YEUTTER. In my judgment, structural adjustment, Senator Packwood, has been a part of this Nation's economic philosophy for 200 years.

The CHAIRMAN. Structural adjustment means what?

Ambassador YEUTTER. It means that not everyone can survive, either in the way of industries or firms. Now, there has to be a qualification of that, based upon national security, of course.

The CHAIRMAN. Skip that for a moment, because I think all of us would agree that national security is an exception.

Ambassador YEUTTER. All right.

The CHAIRMAN. We might argue whether certain industries are critical or not of the national security; but for the moment, stick to the ones that most people would not think are critical to the national security because the fundamental question we are coming down to is whether we are going to protect those industries. They may say they want 5 years for adjustment, but we all may know that 5 years for adjustment isn't going to do it.

Ambassador YEUTTER. Yes.

The CHAIRMAN. Should our position be to gradually ease those industries out—whether it is with trade adjustment assistance to help the workers—but not attempt to maintain them?

Ambassador YEUTTER. I have said on a number of occasions, Senator Packwood, that I do not believe there is a compelling need for the United States to make everything that exists in the world. There are some products that we simply need not produce here in the United States. So, in those instances, perhaps a phaseout is appropriate. I would really put a qualifier on that, though, in that there are niches in almost all industries where people can be competitive and can survive. Using footwear as an example, I am personally convinced, Mr. Chairman, that there is probably a 20-percent segment of the U.S. footwear demand that will always be met by U.S. firms. So, even in that industry, which is very labor-intensive, where our international competitiveness has weakened dramatically in recent years, there are some viable profitable niches.

The CHAIRMAN. I understand that; and those are the ones that won't need the protection against the wage differential, anyway.

Ambassador YEUTTER. Precisely.

The CHAIRMAN. Now, for the ones that don't, we simply ease them out?

Ambassador YEUTTER. Yes, sir.

The CHAIRMAN. Let me finish this then. If a case is then brought before the International Trade Commission under section 201, injury is found; and we all know that the industry is indeed injured by the wage differential, but they are going to be injured in 3 years and they are going to be injured in 6 years and they are going to be injured in 9 years. And they are not critical to the national security. Should the President then be left with the authority to not invoke the International Trade Commission recommendations because he is balancing off additional interests; and he is saying that, even though that industry is injured and I understand that, in our overall national interest, they should not be saved?

Ambassador **Yeutter**. Yes, because structural adjustment, Mr. Chairman, is a painful process. If we make a national decision—and this would be a decision by the President in the case you cited—that we, the United States, should go through the structural adjustment for that particular industry, which essentially means a phaseout, then we ought to do that with compassion and with rational good sense. And that gets into the adjustment assistance question that Senator Moynihan raised, training issues, and whatever else is essential to making that process as painless and humanitarian as possible and as effective as possible.

The **Chairman**. Thank you very much. Senator Chafee.

Senator **Chafee**. Thank you, Mr. Chairman. Mr. Yeutter, in your statement you discuss the deficit, but I don't believe you touched on the deficit in your remarks. Your predecessor said that he felt that about 60 percent—and we know it is hard to quantify these things objectively—of our trade problems were due to the national imbalance in our budget, our Federal deficits. Would you go along with that?

Ambassador **Yeutter**. That is certainly a ballpark figure, Senator Chafee. There have been a number of studies on that recently, including one by Fred Bergstrom that some of you may have seen that focuses on this; and his numbers are in that ballpark.

Senator **Chafee**. I would hope that, in all the public statements that you make that would continually be brought before the public. Somehow the suggestion is out there that we are weak-kneed pantywaists; that we are just not enforcing our trade laws; and if we would get in there and be tough, this thing would all straighten out. The truth of the matter is that the trade deficit is due to our own excesses in Federal spending, at least 60 percent—or over 50 percent—of our troubles trace right back to our budget deficits.

Ambassador **Yeutter**. There is no question, Senator Chafee, that that is the major issue; and there is no question in my mind but that the Federal budget deficit accounts for most of the explanation.

Senator **Chafee**. Now, on these matters that aren't covered by GATT—intellectual property, investment, and so forth—you indicate that even though they are not covered by GATT, we are going to move forward with them and do something about them. As I understand it, though, in your statement somewhere you said that you will be coming forward with ideas on what to do about these matters on a bilateral basis?

Ambassador **Yeutter**. If necessary, yes. We would still like to go the GATT route with a new round, as I indicated. That is the preferred course of action; but if those discussions bog down in Geneva 2 weeks from now to where it becomes evident that a new GATT round is not likely to occur, or simply could not occur with those issues included, then we would prefer to pass on a GATT round. In our judgment, this is not a negotiable issue. Services, in particular, must be in the round or we are just not going to have a new GATT round from the U.S. standpoint; and we will have to confront those issues in a different way—pluralaterally or bilaterally.

Senator CHAFEE. The thing that bothers me, Mr. Ambassador, is that anything to do with GATT takes so long. If we embark on a new GATT round and even if things worked out in a splendid fashion, nonetheless—being completely realistic—the new GATT round would take how long? Two or three years at a minimum?

Ambassador YEUTTER. Yes, at least that.

Senator CHAFEE. All right. So, I don't understand the reason for delay in taking action on this intellectual property business.

Ambassador YEUTTER. I may have misled you, Senator Chafee. We will proceed on a bilateral course as well.

Senator CHAFEE. You will?

Ambassador YEUTTER. Yes. They would be complimentary.

Senator CHAFEE. Some of the violations are taking place with countries that have a mammoth trade surplus with us and that means we have some leverage with. I suppose the worst offender is Taiwan, isn't it?

Ambassador YEUTTER. Yes, I would place Taiwan No. 1 on that list.

Senator CHAFEE. Who is No. 2? Korea?

Ambassador YEUTTER. Probably Korea. Yes.

Senator CHAFEE. I just think that is so clearcut. Now, are there international ground rules of some type that we can follow, or are we solely using arbitrary U.S. standards? In other words, on intellectual property there are international copyright laws of some type, are there not?

Ambassador YEUTTER. Yes, but they are very limited. Senator Chafee, and some of them are in organizations to which we are not a signatory. So, they are of no consequence to us. There are some who feel we should be a signatory to those institutions, but that is another complicated question in itself. So, basically, our ammunition lies with section 301 at the moment.

Senator CHAFEE. Now, you mentioned—I believe in answer to Senator Moynihan, if I understood it correctly—that something critical is going to take place in the next few weeks in connection with GATT. Is it Geneva you are going to?

Ambassador YEUTTER. Yes. This is the annual meeting of the GATT contracting parties.

Senator CHAFEE. And that is where the decision will be made whether to go ahead with a new round?

Ambassador YEUTTER. The decision will be on the first step, which would be establishment of a preparatory committee.

Senator CHAFEE. All right. Now, can you only move with unanimity, or how does that work?

Ambassador YEUTTER. Traditionally, that has been the case, Senator Chafee. There is nothing that requires that. In other words, there could be a vote; and if there is a vote, we are convinced that our view will prevail, that the vast majority of GATT members will support a new round; but that would be a departure from tradition where the GATT has operated on a concensus basis.

Senator CHAFEE. Now, one final question, if I might, Mr. Chairman? In your statement, did you say that nations representing 95 percent of world trade are prepared to proceed with a new GATT round?

Ambassador YEUTTER. That is correct.

Senator CHAFEE. I think if you have 95 percent of anything, you have a good head start. I would hope that, even though you are not meeting your traditional requirements of unanimity, you will plunge ahead. I would hope the other nations would also; and those that don't want to play, what becomes of them? What happens to them?

Ambassador YEUTTER. They would certainly be outside of the scope of any new arrangements that would be negotiated, and then we would obviously want to consider our relationship to those nations on a bilateral basis, too. GSP privileges is an example. One must wonder how generous the United States should be with GSP privileges for nations that are, in our judgment, attempting to torpedo the international system. So, there are a lot of questions that will arise, both within and without the GATT, as to how those nations would be treated.

Senator CHAFEE. Thank you, and thank you, Mr. Chairman.

The Chairman. Senator Long.

Senator LONG. I was told the other day, Mr. Ambassador, by someone in the steel industry who said that this industry can compete successfully in its own market—which is the United States—if we could prevent other nations from subsidizing their steel exports. Do you think that is correct or not?

Ambassador YEUTTER. I am not enough of an expert on the steel industry, Senator Long, to give you a credible answer; but I would say that at least that is a solid argument, and in my judgment, it is a proper course of action, irrespective of whether it is accurate or not. In other words, if we can provide them that kind of level playing field, then let's let the market decide whether or not they really can compete. They would certainly have no cause to complain to you or to me if we gave them that kind of an environment; and then, if they could compete that would be great. If they cannot compete, then we as a nation would have to reappraise the entire situation.

Senator LONG. The steel industry is important for the defense industry, if for no other, but I do think that it would be a good thing to know. Would you look into that in greater detail and send me some communication on that subject, as well as whether or not you think that this industry could compete effectively? I know there is a big difference in the price of foreign and domestic steel.

Ambassador YEUTTER. I would be happy to, Senator Long. To some degree, as you know, that question is moot now in that the present steel program that is in effect puts quotas on all the importing nations, that is those that export to the United States, all the way to 1989.

Senator LONG. Right. Now, I am concerned also about national resource subsidies, both in timber and in natural gas. Now, there is an area where we can compete. I mean, we can very well compete in our own market; but we can't compete if we are going to let them export a product to us where natural gas is 85 percent of the cost of the product here and they put it in there at a virtually zero price. They won't sell the gas to us for that; they demand a great deal more. So far, I haven't been able to persuade the administration to take the attitude that we are being beat by a natural resource subsidy that we ought to take action against. The same thing exists with regard to what the Near East is doing; and those people are not a member of GATT. They are not abiding by any rules of trade that we support. It is the same thing as selling the gasoline cheaper than they would sell the oil from which the gasoline is made. Now, how can we compete against that if this Nation doesn't uphold the side of its own people? I am talking now about situations that are capital intensive. I have always thought that that was an area where we ought to prevail.

Ambassador YEUTTER. Senator Long, I have a great deal of empathy with your views on that subject. That does not necessarily mean that the administration will support a natural resource bill, but that is a somewhat different question. But if one simply limits the discussion at the moment to the concept that is involved, I have to say to you that there is a practice there that either is an unfair trade practice or it comes awfully close to being an unfair trade practice. It depends on how one defines it. It is a bit difficult, though, to fit within the present jargon of international trade because it is not really dumping and it is not really a subsidy countervaling duty case. It doesn't quite fit the brackets; but nevertheless, it is a troublesome economic practice, and it seems to me that we have to figure out the proper way to deal with it. And you are articulating the problem very well. We are spending a lot of time on that right now, Senator Long, and I have stimulated a lot of discussion within USTR on the point; but we haven't drawn any definitive conclusions yet. It is a live issue, both with respect to the petroleum area and with respect to lumber; and we are getting a little closer, I think, to convergence of thinking. It is an issue that I assure you, Senator Long, is not going to go away. We are going to confront it in some manner.

Senator LONG. Now, the President isn't just talking about free trade; he is talking about free and fair. And I would like to know what in the devil is fair about letting those people put us out of business by subsidizing their product, a natural resource for a far lower price than they would sell it on the world market.

Ambassador YEUTTER. As I said, we have got a lot of work underway on that. There is a lot of interest internationally in this, too, Senator Long. It is not just the United States; and in fact, that subject is one of the issues that will be on the agenda for the Quad Meeting, which is a meeting of the trade ministers of the European Community, Japan, Canada, and the United States, which I will host in San Diego in January. So, we will have those four major trading partners dealing with this issue in some depth in January in San Diego.

Senator LONG. But if you are against discrimination and you are against subsidies, especially where it is costing us jobs, it seems to me you are going to have to do something. Otherwise, don't be surprised to find that the people who wouldn't be voting with you will be joining the other team.

Ambassador YEUTTER. It is a complicated question, Senator Long; and the response of the other nations, of course, is that you Americans don't have any right to tell us how to price our natural resources. That is a sovereign decision for us to make; it is not your prerogative to tell us; or, alternatively, if you are going to tell us how to price our resources, we are going to tell you how to price yours.

Senator **Long**. We sure have the right to tell them what comes in this market.

The **Chairman**. Senator Grassley.

Senator **Grassley**. Thank you, Mr. Chairman. Mr. Ambassador, I want to address generally the issue of agriculture and foreign trade; and I am sure you would expect me to ask you about that. I would like to have some sort of general overview from you of where agriculture fits into the entire work that you are doing and how that might be different with you than it was with your predecessor. And would you say that particularly from the standpoint of your interest in the previous administration with foreign trade as an Assistant Secretary of Agriculture? I guess I am asking it in light of what I have here, where statistics show a rapid decline of agricultural exports from $44 billion in 1981 to $34.5 billion in 1985. That is a 22-percent drop. An example would be that we used to furnish all of the feed grains to the Korean market. Today, the United States is providing very little. Australia has taken over because they can provide Korea $20 per ton below the United States price for corn. China is shipping 700,000 tons of corn to Korea. And Korea is just one country; and I don't want you to dwell on Korea. You can forget about that, but at least you know where I am coming from.

Ambassador **Yeutter**. I would be happy to comment, Senator Grassley. As you know, we have both spent a lot of time on the question of agriculture through the years. What has happened in the last several years is certainly bordering on tragic for American agriculture because, as an industry, it has become so export dependent and properly so. Our domestic market is not growing in any substantial way because our population is increasing slowly in the United States today. So, the only way for us to have an economically viable and healthy American agriculture is to export and to export very substantial quantities of product. That has been increasingly difficult in recent years because of the very strong dollar. Unfortunately, from agriculture's standpoint, as you fully appreciate, Senator Grassley, we sell mostly raw product on the export market. We don't sell much in the way of brand name agricultural products. We sell corn and wheat and soybeans, and that means price is the determining factor as to whether a buying nation comes to our store or to somebody else's store. And with a very strong dollar, we have not been price competitive. To some degree, this has also been due to price support levels that have priced us out of world markets; but for a combination of reasons, we have lost market share in recent years, and that has had a devastating impact on farm income. The question then becomes: What can we do about it? And I would say, to summarize it in a few seconds, Senator Grassley, that the most important contribution any of us can make to that cause is to provide a macroeconomic environment internationally, the result of which will be a decline in the value of the dollar and an increase in our international competitiveness for agricultural products. We have made a lot of progress in that regard over the last 6 or 8 months. The dollar is substantially lower today than it was a few months ago. We are substantially more competitive, but we are not going to see that reflected in agricultural export numbers until next year, at the earliest. And as you know, there is an enormous amount of surplus in existence in the world.

Senator GRASSLEY. Let me get you to focus in on something before my time is gone. I am more interested in your negotiations and how your present approach is any different from your predecessor, and where does it fit in?

Ambassador YEUTTER. All right. The present approach is more aggressive, Senator Grassley, not just on agriculture but on other issues as well. We have had some major confrontations with the European Community recently. As you know, we have just filed a GATT case against their export subsidies on wheat, and we have some other controversies going with the Community on agriculture. In addition, we are moving toward a major GATT negotiation on agriculture, presuming we get a new GATT round launched; and that, to me, Senator Grassley, is probably going to be the critical negotiation for American agriculture.

The CHAIRMAN. Senator Symms.

Senator SYMMS. Thank you, Mr. Chairman. Mr. Ambassador, I want to pursue from where Senator Long left off, if we can shift back to that. Of course, coming from an agriculture State. I am also concerned about the agriculture question. But I hear the commentary all the time by the economists and others that espouse free trade, that we don't want to get into a trade war. I go into my own State and see sawmills that are under tremendous pressure from Canadian timber, and I see semiconductor producers laying off thousands of workers. It looks to me like we are already in a trade war, and we are losing it. What kind of a timeframe do you have? When are we going to see some kind of action on the question of timber, on the question of semiconductors? Is there going to be any action?

Ambassador YEUTTER. A short timeframe, Senator Symms, and I know that is music to your ears because those are significant issues in your State and areas where you are suffering financial deprivation at the moment. If I may, I will hit both of those issues very quickly just to give you an update. Timber is an issue that we must resolve. There is an enormous amount of interest in that question within the United States, not only in your part of the country but through the South as well. And as you know from the U.S. ITC report on timber, it is apparent that stumpage rates in Canada are 10 percent or thereabouts of stumpage rates in the United States. That has a lot to do with timber flows across the border. We have that same philosophic issue before us that I was discussing with Senator Long, but nevertheless, there do seem to be some aspects of the stumpage calculations in Canada that are certainly questionable at best. In addition, we have timber issues with Canada, as you know, on plywood standards, which affect flows going from here in that direction—their tariffs on timber, export controls on timber. I really believe we are heading, Senator Symms, toward a negotiation with the Canadians on this subject, although I have not had a chance for discussions in recent days with my counterpart, Mr. Kelleher, because he is in Australia and won't be back for a few more days. We have had a lot of discussion within the administration internally on that, including a trade policy review group meeting as recently as yesterday; and I believe we are coming very close to having our own position in order and probably initiation of a negotiation with the Canadians.

Senator SYMMS. That is on timber?

Ambassador YEUTTER. That is on timber. On semiconductors I was in contact with people in Japan as recently as this morning, and we have a team going to Japan next week, led by Ambassador Mike Smith, my deputy. We anticipate a serious negotiation with the Japanese on semiconductors, or the 301 case that is now before us next week—not a definitive one, but a very serious one in which a number of proposals will be on the table from the Japanese. And I am still hopeful that we might get a negotiated result with the Japanese. There is a small chance that it will be by the end of the year, but more likely early next year. Now, what that result will be is too early to determine; but without question, we have generated their attention on that issue and we recognize, Senator Symms, how important this is to the U.S. industry, which is hurting badly at the moment.

Senator SYMMS. It seems to me that there is also a security implication. It becomes rather critical when we have plants that make semiconductors going out of business. We have been and are still, in my opinion, the leading edge of technology in that entire field. So, the sooner we get it fixed, the better. A lot of my constituents say we should just shut the door on their products coming in here until they open the door on, say, beef, tobacco, oranges, apples, and potatoes. What do you say to those kinds of comments?

Ambassador YEUTTER. In the middle of the negotiation, that would not be a responsible course of action. If the Japanese were not negotiating with us or discussing these issues in good faith, I would say that that might be an appropriate response; but I have no indication to believe at this point, Senator Symms, that they are not working just as hard as we are to come to a sensible conclusion. So, I would prefer to give them the benefit of the doubt, at least for a time.

Senator SYMMS. But you are talking about, in terms of timber, even this month? And semiconductors early next year? Some position?

Ambassador YEUTTER. Yes. Now, with timber, of course, we won't have a result that quickly because the negotiation will take a substantial period of time, but I would hope that we could get something going shortly.

Senator SYMMS. Thank you very much. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Danforth.

Senator DANFORTH. Mr. Yeutter, in your discussion with Senator Packwood, you stated that there are certain industries that are just not competitive. They can't compete and they should be phased out. That was my understanding of your testimony. Do you believe that textiles is a dying industry that should be phased out?

Ambassador YEUTTER. No.

Senator **Danforth**. No? That was my understanding of what you said.

Ambassador **Yeutter**. That is the problem with generalizing, of course. There are certainly segments, Senator Danforth, of the textile industry that probably cannot be competitive with their counterparts in the Far East, but I certainly would not draw that conclusion for the entire industry by any means.

Senator **Danforth**. There might be some residual parts of the textile industry that could survive?

Ambassador **Yeutter**. A very substantial residual in my judgment on textiles. Maybe a smaller residual on the apparel side, but as you know, our textile industry is really quite modern and quite efficient.

Senator **Danforth**. Do you think that there are segments of the textile industry that should be phased out, that can't compete?

Ambassador **Yeutter**. That is inevitable, in my judgment, because of some of the smaller operations that are very labor intensive; and it seems to me that ultimately, in the society in which we live, that would result.

Senator **Danforth**. And in apparel, you think that there is somewhat more in the apparel area that could just be phased out?

Ambassador **Yeutter**. Simply because it is much more difficult to move to factory-type automation in apparel than it is in textiles.

Senator **Danforth**. In steel?

Ambassador **Yeutter**. In steel, I would draw a different conclusion. Steel is plagued not by labor-intensivity, but by relationships of wage rates to productivity; and indications are that the industry is moving to correct its course there. I am much more optimistic about the long-term viability of the American steel industry.

Senator **Danforth**. Footwear?

Ambassador **Yeutter**. Footwear, as I indicated earlier, I really believe there is a 20-percent market share or so that is really quite solid and will be a niche maintained by U.S. firms for a long time to come. The other portion is already——

Senator **Danforth**. Can't compete and should be phased out?

Ambassador **Yeutter**. Well, it is already phased out, by and large.

Senator **Danforth**. How about copper?

Ambassador **Yeutter**. Copper is an industry that is having difficulty competing. Copper may well have national security considerations at some point in time that merit our concern and your concern; but aside from that, my judgment is that the copper industry really must learn to compete in the long run.

Senator **Danforth**. Do you think that it can compete, or do you think that it can't compete and should be phased out?

Ambassador **Yeutter**. Prospects at the moment do not look encouraging; but whether the industry or individual firms can compete or not depends a lot on the management skills of those firms, the technoloy they follow, and a lot of other factors that are within their control.

Senator **Danforth**. Don't you think that if it is in doubt, we shouldn't just kiss off an industry, but instead we should try to provide some opportunity for it to restructure itself, regroup, and become competitive? Maybe we should. Maybe the administration's position is that, if there is doubt, we should take the position that basically we don't think they can compete, and we should just let them be phased out. But my guess is that you would say that, if there is some doubt, we should give them an opportunity to rebuild themselves and to become competitive.

Ambassador YEUTTER. That is a decision that will obviously have to be made on an individual case basis, Senator Danforth, and the decision may well be different in 1985 from what it might be in 1990 or might have been in 1975 because the underlying fundamentals will change. But yes, if there is a realistic chance of the industry restructuring itself and becoming internationally competitive, we ought to give them that chance. If it be the judgment of the President of the United States in that particular situation that there is no realistic chance of adjustment or of recovery and restructure, then they should be phased out.

Senator DANFORTH. It is a kind of a negative Humphrey-Hawkins approach, that the President decides that some industries just aren't competitive and can't survive and just phase them out; but perhaps there are others that can survive.

Ambassador YEUTTER. The ultimate decision, Senator Danforth, will be made by the industry itself. We shouldn't have Government providing that function. That responsibility lies on the shoulders of the CEOs in that industry, and it is a question of whether the Government is going to preserve them.

Senator DANFORTH. Absolutely. I mean, nobody can do this for industries, but the whole reason for section 201 of the Trade Act is to provide a kind of a phasing, a kind of a cushion. Wouldn't you say that the present state of section 201—you and I have agreed on this in the past—that given the shoe decision, the present state of section 201 is that it is a dead duck.

Ambassador YEUTTER. Now, that is an overstatement, Senator Danforth, in my judgment.

Senator DANFORTH. A skinny, aged, and wounded duck?

Ambassador YEUTTER. No, there has to be a judgment call made under section 201 by the President of the United States; and that judgment call, in my opinion, is properly made upon consideration of a host of questions that reflect the national economic interest. And simply because the footwear case was a negative does not necessarily mean that all other cases will provide a comparable result.

Senator DANFORTH. It is widely taken to stand for that proposition. I am sorry, Mr. Chairman. I will be happy to wait for the next round.

The CHAIRMAN. We are going to have another round. Senator Pryor.

Senator PRYOR. Thank you, Mr. Chairman. Back to the issue of agriculture, Mr. Ambassador. I hope very much that, in your new role, you will pursue an area that concerns me deeply and, I think, concerns all Senators and Congressmen from agriculture States. Let's take Brazil. About a dozen years ago, our United States Department of Agriculture went to Brazil and said: "All right, friends, here is how you grow soybeans." We teach them how to grow soybeans. Then, our Commerce Department went down there and said: "OK, now that you know how to grow soybeans, here is how to market soybeans." And now, after the U.S. Department of

Agriculture and U.S. Department of Commerce have been involved to a very great degree, the State Department, through the Agency for International Development, goes down there and helps build the roads to get these soybeans out to the ports for export.

I don't know how many millions of taxpayers' dollars we have used in these efforts, but in the case of soybeans, at least, we are not talking about the high dollar, and we are not talking about low wages: We are talking about using our tax dollars to subsidize the Brazilian soybean industry. As a result, they are taking over the market. I think, where we used to have 70 percent of the market, other countries—Argentina, Brazil, and on down the line—have taken that market away from us. I hope that you will use your good offices and your influence to look into how American dollars are subsidizing the Brazilian soybean farmer and other farmers. This is something that certainly I would appreciate having information about. I think it is an enormous problem, and is very, very significant in terms of dollars and also of our presence there.

Ambassador **YEUTTER**. We would be happy to evaluate that, Senator Pryor. I haven't looked at the particular situation in Brazil recently, but I would add to your littany of considerations there, the fact that probably the greatest motivation we provided for production there was our embargo on soybeans back in the early 1970's which stimulated a whole lot of Japanese investment in soybean production in Brazil. That may have been the single most important factor. So, we may have shot ourselves in the foot in a number of ways in that and in other areas around the world. I can recall when I was in Government in 1977 that we had a substantial discussion about doing the same kind of thing through stimulating palm oil production in Malasia and a number of other countries in Southeast Asia, with the palm oil then, of course, also coming into competition with soybean oil exports at that time. So, this is an issue that arises not only with respect to soybeans but with other issues as well; and what it means is that we need to be circumspect and cautious about our own self-interest in loan programs and grant programs, whether they be AID or through the international lending institutions, such as the World Bank and the regional development banks. So, that is a legitimate point; and we will be glad to give you any inputs we have on the present Brazilian situation.

Senator **PRYOR**. And by the way, I would appreciate getting that as soon as possible, and I know other members of this panel would, too. I see the warning light on, and I will have, Mr. Chairman, some written questions on the Canadian timber industry and what it is doing to Arkansas timber industries. I will just submit those to the Ambassador in writing.

Ambassador **YEUTTER**. That would be fine.

Senator **PRYOR**. Thank you very much.

Ambassador **YEUTTER**. Thank you, David.

[The questions submitted by Senator Pryor and Ambassador Yeutter's responses thereto follow:]

Question. A number of industries have been hit hard in recent years by imports. Among those is the furniture industry, which has seen imports rise over 40% in the last year alone, and 284% from 1979-1984.

In recent years one of the most difficult trade problems for the furniture industry has been the severe trade deficit with Canada. Canadian exports to the U.S. have more than doubled since 1980, while U.S. exports to Canada have actually declined. U.S. furniture exports to Canada in 1980 were $107 million, and declined to $93 million in 1984. One major cause of the problem is inequitable tariffs. U.S. furniture entering Canada faces a 16.3% levy, while Canadian furniture entering the U.S. faces duties as low as 3.1%. I understand that there will be trade negotiations occurring between the U.S. and Canada in the near future. What would you do at USTR to resolve this problem that is extremely important to over 10,000 of my constituents?

Answer. We expect that the Canadian Government will propose the initiation of discussions on a comprehensive trade agreement with the United States this fall. Over the last year, we have made it abundantly clear to the Canadian Government that we want to include the furniture sector in any future discussions of this nature. As USTR, I will continue to press for the elimination of Canadian tariffs on furniture as part of any comprehensive trade agreement with Canada.

Question. There is mounting concern within the agricultural community about growing imports of agricultural products exported from other countries with the aid of export subsidies. Present procedures for combating these imports appear to be slow and cumbersome. Would you support legislation to streamline these procedures and make them more effective against such imports?

Answer. Since the U.S. countervailing duty laws were changed in 1979, neither we nor the department of Commerce are aware of any complaints by U.S. agricultural industries with respect to timeliness of process. If the Senator knows of any specific complaint, I would be happy to look into it. Under existing law, if the preliminary determination of subsidy is affirmative, countervailing duties are charged on merchandise entering the United States within two and one-half months of a petition being filed with the Department of Commerce.

As a part of the 1984 Trade Act, there were a number of technical changes made to the countervailing duty laws to streamline them and make them more effective. For example, special offices have been set up in the Department of Commerce and at the International Trade Commission to provide assistance to small businesses in the filing of countevailing duty petitions. Also, the paperwork requirement has been simplified and clarified and should result in a reduction in cost to private parties.

Question. The export credits guarantee program is very important to the rice industry. Do you support the continuation and expansion of the export credits guarantee program? Would you support credit for Nigeria?

Answer. Yes, I support the continuation and expansion of the export credit guarantee program. The Administration in its FY 1986 budget request is seeking approval for a $5 billion GSM 102 program.

In 1984 there was an interagency decision not to advance any more CCC credit to Nigeria until it began to take steps to resolve its economic difficulties. There remain serious doubts about Nigeria's creditworthiness and for this reason I would probably not support giving CCC credit to Nigeria until we have some reasonable assumption of repayment.

Question. As you know, many developing countries with huge debt obligations to U.S. Banks, such as Argentina and Brazil, are also major competitors of U.S. agriculture for international markets. Some of the exports from these countries, such as Brazilian soybean oil, are subsidized through varying exchange rates, export drawbacks, etc. Do you believe it is wrong for the U.S. Government to take action against such exports since they are from countries with large debts to U.S. Banks?

Answer. Unfair trade measures which adversely affect U.S. farmers or businessmen and violate international agreements are wrong and should be addressed, regardless of the financial obligations of the countries which employ those practices. In fact, with specific regard to Brazil, USTR is currently pursuing a Section 301 action involving Brazilian subsidies which benefit oilseed crushers.

In response to a petition filed on April 6, 1983, by the National Soybean Processors Association, USTR has charged that Brazilian subsidy practices distort international markets for soybeans and soybean products and disadvantage U.S. exporters. The U.S. requested consultations with Brazil on this matter under Article XXII of the GATT. Initial consultations were held in Geneva in November of 1983. Follow-up consultations are scheduled to be held on July 31 in Brazil. A number of changes have been implemented in Brazil's subsidy programs since the Section 301 case was initiated in 1983. The purpose of the upcoming discussions is to clarify the effects of those changes and provide the basis for evaluating the need for further action on this case.

Also, both Brazil and Argentina maintain differential export tax systems for oilseeds and oilseed products which USTR has identified as trade distorting practices. To encourage domestic processing, export taxes for oilseeds are substantially higher than those levied on oilseed products. The effect of these tax schemes is to artificially restrict exports of oilseeds and increase exports of oilseed products. U.S oilseed processors have charged that these practices provide an unfair benefit to Argentine and Brazilian processors. We are now pursuing this matter bilaterally. USTR has raised this issue on a number of occasions with both governments and argued for an elimination or substantial narrowing of the tax differentials. High level trade talks are scheduled with both of these governments during July. Their differential export tax schemes for oilseeds and products will again be raised during those talks.

The CHAIRMAN. Senator Bentsen.

Senator BENTSEN. Thank you very much, Mr. Chairman. Mr. Chairman, during the Ambassador's confirmation hearing, I asked him to give us a report under section 305 on some of these trade abuses; and I am looking now at the National Trade Estimate that we received on October 30. I was the sponsor of the legislation to require the National Trade Estimate, Senator Chafee and Senator Bradley cosponsored that bill. The report contains extremely helpful information. Let me say, Mr. Ambassador, I am very appreciative of the expeditious way that you prepared this report and delivered it, in spite of your workload. But now having said that——

Ambassador YEUTTER. What have we done with it?

Senator BENTSEN. Yes. You have 250 pages there of trade barriers that we are talking about; and what we have seen thus far is that the President has resurrected four antique trading disputes under section 301. It will probably take at least a year for those cases to bear say fruit. And if we win you may see an increase in U.S. exports of probably $300 or $400 million a year.

You gave us an estimate for the value of about 15 percent of those barriers. That is a small percentage, but even so, the loss in exports amounts to about $4.5 billion a year. So, it is obvious that we have to do a great deal more than we are.

I agree with you that we have shot ourselves in the foot around here on a number of trade issues. I think President Nixon did it on the ban on the export of soybeans; and President Carter did it on wheat; and I think President Reagan did it on the pipeline. I think the French and the Japanese enjoyed that very much, because they filled the gap we left.

What I am asking you is, just what you said. What are you going to do now?

Ambassador YEUTTER. Excellent question, Senator Bentsen. First of all, thank you for the kind comments with respect to the report, not just that you made this morning but publicly at an earlier date as well. It is a report that took a great deal of work and a lot of midnight oil to meet that October 31 deadline, but I am pleased we got it done.

Senator BENTSEN. It came in pretty handy for the administration, though, when they began to change their position on trade.

Ambassador YEUTTER. Yes, it did. Yes, it did. [Laughter.]

There has to be some self-motivation occasionally. Nevertheless, it is a valuable piece of work; and we now are concentrating on where we go from here. We have an internal working group, Senator Bentsen, that is developing plans right now for how we are going to organize to handle the followup, and we will share with you that structure as soon as we put it in final form. There have already been some meetings on the subject, and we should have something to say on that within the next week or two. One decision will be how much of this will be handled by the strike force and how much of it will be handled internally within USTR. Then, also the question of how we add to that report in the future. As you know, much of that has been——

Senator BENTSEN. That is quite a workload. Is that going to require more staff?

Ambassador YEUTTER. It is too early to tell, Senator Bentsen. Obviously it will be difficult to sell additional funding anywhere within Government these days, so we would have to make a compelling case for new staff or new support if we really felt it was necessary.

Senator BENTSEN. Let me interrupt again, if I might, because of the time limitation here. I would have been here earlier, but I have been assured since 10 that an amendment I was interested in was going to be up any moment, which has not happened. I understand that you said earlier that GATT is in danger of breaking down.

Ambassador YEUTTER. Yes, I did.

Senator BENTSEN. Some of us have introduced a bill—Senator Baucus, Senator Moynihan, and a number of others.in which we call for a strengthening of GATT, a restructuring of GATT, making that one of the primary objectives in the new round of multilateral trade negotiations. I would like to hear you address that. GATT needs real penalties, that actualy go into effect.

Ambassador YEUTTER. I couldn't agree more with that. I have had a lot of debate, Senator Bentsen, with our European Community colleagues in particular on that point because it just seems to me we cannot continue to function the way we are now. GATT is not a credible institution today because it doesn't deal with issues. It just simply foists them off. It provides a mechanism for people to fend off attacks, rather than resolve issues. Now, I have had this discussion with Arthur Dunkle, the Secretary-General of GATT, and I have had it with a number of our other trading partners as well, including a lengthy discussion at the last quad meeting up in Canada. And I said to our major trading partner, Senator Bentsen, that in my judgment we have got to not only improve the GATT in this new GATT round—the next GATT round—we have got to improve it by quantum leaps, not incrementally. This time we need a quantum leap, and we have got to get the commitment of the major trading partners to make that quantum leap. It is important, or the GATT is not going to survive very much longer as an institution. All of this fits into that process because a lot of the issues that have surfaced in this report really should be dealt with in the GATT; and I hope we can do that. But you have focused, Senator Bentsen, on what I believe is the most critical trade issue for the world today.

Senator BENTSEN. Thank you.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. Since it is the most important issue in the trade world today, let's continue on it. I assume that you are addressing to some degree the dispute settlement mechanisms in the GATT?

Ambassador YEUTTER. Yes.

Senator BAUCUS. I think it is clear that most people in this country think GATT is a farce. Nobody pays any attention to it. It is self-serving; they don't want to make any decisions. It is worse than most prerogative connotations of a country club. I mean, there is just nothing to it at all. So, what are some of your thoughts as to how we can put a little bite and teeth into the dispute settlement mechanisms? What do we do? What are your preliminary thoughts on how we beef it up a little bit—that part of it?

Ambassador YEUTTER. One of the things that I have done, because I felt so strongly about that when I came, Senator Baucus, was that I put together a little working group to evaluate that question. That working group is chaired by Jules Katz, former Assistant Secretary of State, who is one of the most respected people in this business. And I asked him to chair a group composed of a variety of people outside of the Government that would look at this, including labor union representation that is on it, because I felt that there was nobody who has greater experience in dealing with disputes than labor unions. So, we have that kind of input also. I wanted him to get some creative thinkers together and focus on how we can shape up the dispute settlement mechanism of the GATT. They have been meeting in recent weeks, and Mr. Katz is coming in to give a preliminary report to me next week. So, I can give you a better answer after I have talked with him. I have not talked with him since I have established the group.

Senator BAUCUS. I have a hunch that, whatever he says, you are going to have to beef it up even more. You know, a lot of people say that the letters G-A-T-T really stand for "Gentlemen's Agreement to Talk and Talk," and that is what it is.

Ambassador YEUTTER. Yes; right.

Senator BAUCUS. There is a lot of talk and no action.

Ambassador YEUTTER. No question about it, Senator Baucus. The two major challenges in that area, I think, just to articulate them, are the need to have it be expeditious and decisive. Today, it is neither.

Senator BAUCUS. Whatever your group comes up with, I will bet you dollars to doughnuts that you are going to have to increase the teeth in it—sharpen the teeth tenfold because it is not going to be enough. I also wondered, as we explore new GATT rounds, really what you think about focusing on some of the points that Senator Danforth brought forth. There is sort of a disquieting and a worrisome, haunting feeling here that some industries are going down the drain; and we might let them go down the drain because foreign wage rates are so much lower than they are in this country. Now, obviously, there are some niches, as you mentioned, that we can take advantage of, and obviously there are some adjustment processes that you have to define and explore to make them work better. In addition to that, it seems that lower wage rates might sometimes be an unfair trade practice particularly when the labor conditions are so poor in some countries, even by those countries' standards; and that might constitute an unfair trade practice. Don't you think that that should also be included in the new GATT round?

Ambassador YEUTTER. I am not sure how we would handle that issue, Senator Baucus. I am openminded enough to say that I am amenable to listening to arguments on that point. I would not wish today to take a position on that issue. It seems to me that we ought to be openminded enough to consider anything that might impede trade.

Senator BAUCUS. I encourage you to look at that very, very closely. Finally, one other matter here. I will be now the fourth Senator that you will hear this morning who will ask you to move much more quickly and decisively on timber. You wrote us saying that you couldn't do much until the report came out. The report has now been out, and it is outrageous, frankly, what Canada is doing on stumpage. You know better than I that it is going to take a lot of work and a lot of tough work if we are going to resolve that successfully because Canada is balking very, very strongly at any actions we are taking. I want you to know that many of us here—and enough of us here to take any action that has to be taken to force Canada to back off its subsidy of its timber stumpage. And to some degree, the same issue applies to Japan. I mean, we are not getting anywhere on the Moss talks on processing of forest products; we are not getting anywhere. They are just dragging their feet on it—a lot of talk and no action. Again, that is unfair; they know it is unfair. When I talked to the Japanese, you could tell they know it is wrong and it is unfair and so forth; but they are not doing anything about it. They know it is wrong; we know it is wrong. Therefore, because we are on such high moral ground on it, we ought to just do something about it and be decisive about it. Give them an absolute deadline and maybe take some political action against them, in addition to economic action against them. It just seems to me that we are not doing enough in standing up for our rights and certainly on those two issues.

Ambassador YEUTTER. On the latter issue, since I have not commented on it yet, let me just say that, as you know, Senator Baucus, that one has a deadline of the end of the year. USDA has the lead on that one although USTR is a participant in that process. We are just as distressed by that result as you are; and clearly, the United States will have to make a judgment shortly after the first of the year as to how we wish to respond to whatever result there is or lack thereof on the Moss process on forest products.

Senator BAUCUS. Thank you.

The CHAIRMAN. I ask unanimous consent that a statement by Senator Bentsen—an opening statement—be placed in the record following the other opening statements of the members. Without objection. Senator Moynihan?

Senator MOYNIHAN. Mr. Chairman, maybe I should address this remark to you and to Senator Danforth as much as to Mr. Yeutter, which is to say that clearly there is an organizational crisis developing in the GATT. I think it is helpful to recognize that that organization crisis began 38 years ago when this committee refused to have the United States join the International Trade Organization, which was intended to be an organization with a dispute settlement mechanism and other characteristics, good and bad, of such organizations. When this committee turned down the ITO, something had to be improvised, and an inspired Treasury official of Great Britain, Eric Whydham-White, just worked it out. And for 25 years, the GATT consisted of Eric Whydham-White and a few French secretaries; and he worked it out. It was because we rejected an organization that we got this nonorganization, so much so that the poor man—they never even provided him a pension. [Laughter.]

No one has ever done more than Eric Whydham-White for the GATT and world trade and he died a poor man. So, you have got to think in terms of creating an onging organization. I think the committee should help in that. We presumably know something about it, or at least we can listen and help you in it. Can I just say two other quick things? Senator Baucus and the chairman have both mentioned the question of wage differentials, and Senator Baucus just mentioned labor conditions. Could I draw your attention to the existence of an organization called the International Labor Organization? It is the first international organization of its kind that we ever joined. The GATT is now in its original building in Geneva. It is an organization that deals with problems of international trade that arise from differential working conditions. Its raison d'etre is the issue of comparative labor costs. It is the only one of the League organizations we joined. We have been there since 1934. Why not use it? I mean, think in terms of the ILO. Not every organization is around 60 years old; the ILO is, and it helps. One last thing, and please answer me—beside just being agreeable, which you always are. I want to call your attention again to Canada. Now, we have heard four people talk about timber today, and there is obviously a problem; but our President and the Prime Minister have made a real commitment to expand United States-Canada trade. Secretary Schulz was out in Calgary, was he not, with his counterpart, Mr. Clark?

Ambassador YEUTTER. Yes.

Senator MOYNIHAN. And you are going to begin negotiations early next year?

Ambassador YEUTTER. We certainly hope so, Senator Moynihan, and I am glad you brought that up because it does seem to me important to draw a distinction between short-term bilateral issues and long-term bilateral issues. Even though we do have some stresses and strains in these short-term issues—timber, pharmaceuticals, pork, and a number of others—it is important to——

Senator MOYNIHAN. I mean, distinctions between live and dead pork is one thing, but Canada is our largest trading partner. It is the most important country in the world to us.

Ambassador YEUTTER. Yes, it is; and what has been proposed by Prime Minister Mulrooney is, in my judgment, truly historic. The potential benefit to both nations of achieving what might essentially be a free trading community between the two is phenomenal.

Senator MOYNIHAN. Could I ask you to hold right there? I want to get the chairman's attention on this. In your testimony, you say that some members of this committee have already suggested that we delay free trade negotiations until our present bilateral disputes are behind us. I hear you are saying "No" to that. In Ottawa, I went up and visited with Mr. Kelleher, your counterpart. They specifically have not proposed a free trade area, and I think they specifically do not like that term; and maybe we could reciprocate by saying we will call it whatever they want to call it. We do agree with Mr. Mulrooney. He wanted an agreement involving the broadest possible package of mutually beneficial reductions in tariff and nontariff barriers. Maybe we could find an acronym for that or something.

Ambassador YEUTTER. Yes.

Senator MOYNIHAN. But that is what we want. I would hope that, if we are not going to start something early next year, you let us know why because I agree with you. This is a real chance—the one real chance we have out there. A President and a Prime Minister want to do something.

The CHAIRMAN. I will tell you a followup on that, though, Pat. I was talking with a very, very, very highly placed Canadian Government official on this issue. I said: Now, you are talking about total exchange of goods—free—right? Yes. Well, I understand that. They have 25 million people. We have 250 million people. As to who is more likely to sell more goods where, they are more likely to sell more goods here than we sell there; and I understand why they support that. And then I said: And you are talking about also a free exchange of investment? Well, no, he wasn't so sure about that; and clearly that would be to our advantage. So, it is going to be a two-way street—not only trade. It is going to be investment if we are going down that route.

Senator MOYNIHAN. That is why we have Ambassador Yeutter. Mr. Chairman, this is what we have in hand. A President and a Prime Minister have said: Let's do it. So, let's do it. Do it right is all you are saying.

Ambassador YEUTTER. Right. We should take advantage of that opportunity because it is historic, and it is important, as you suggest, Mr. Chairman, to make it as broad as possible for the benefit of both countries. I don't want it to be constrictive in any way. There is always going to be a tendency, Senator Moynihan, to say: Well, we mean free trade but, and then start excluding A, B, C, D, E. And I am trying to insist to my Canadian counterparts that they lay everything we can think of on the table and that we do likewise and we proceed from there without beginning to constrain the process.

The CHAIRMAN. Let's move on, Mr. Ambassador, to 301, and unfair; and I am sure we are going to get back to 201 and wage differentials, anyway, in a moment. At the moment, export subsidies and dumping are the two principal unfair trade practices more or less recognized by the civilized trading world. Is that right?

Ambassador YEUTTER. Yes, and there are some others, quota programs for example, and the use of standards in a trade constrictive way when there really isn't a health or safety issue involved. So, there are a number of those, but the principal violations in terms of trade impact are undoubtedly subsidies and dumping practices.

The CHAIRMAN. Yes. Now, under the present law, let alone any new law we may enact, the administration, if it wanted in the administration could define certain foreign trading practices as unfair trading practices, if they chose to do so, even though by international covenant or otherwise they have not been defined as unfair trade. Should we start down that road?

Ambassador YEUTTER. To a certain degree, Mr. Chairman, we do that today under section 301.

The CHAIRMAN. What are some of the areas in which we do that?

Ambassador YEUTTER. Basically, section 301 has language that is sufficiently broad that we can make a unilateral definition. One area in which this theoretically could apply would be the stumpage kind of question in Canada.

The CHAIRMAN. I understand we can do it. Have we done it?

Ambassador YEUTTER. Should we?

The CHAIRMAN. No, have we?

Ambassador YEUTTER. In a sense. For example, we just filed a section 301 case against Korea on services, which is an area that is uncovered by the GATT. So, there is an area in which we have defined——

The CHAIRMAN. We are saying that their preclusion of our services in Korea is an unfair trade practice?

Ambassador YEUTTER. Correct.

The CHAIRMAN. And if we wanted, under 301, we could probably say wage differentials are an unfair trade practice, if we wanted to start down that road.

Ambassador YEUTTER. Perhaps.

The CHAIRMAN. We could probably say that Taiwan's copyright practices are an unfair trade practice.

Ambassador YEUTTER. Correct.

The CHAIRMAN. What will happen if each country starts down the road of defining what some other countries' practices are and says that that is unfair? You alluded earlier that if we tell Canada how to price timber or we tell Mexico how to price gas, they will start telling us how to price electricity. And we have, as you are well aware, in many of this country heavily subsidized electricity. What happens if each country starts doing that?

Ambassador YEUTTER. That is the point I was alluding to in my colloquy with Senator Long. Obviously, that could lead to a very chaotic situation. That, of course, is the rationale of establishing the GATT in the first place and is also the provocation for my comments today that the GATT is demonstrating its inadequacies. As a result of the inadequacies and shortcomings, nations like the United States are moving away from the GATT and establishing their own rules in areas like services; and if we begin to move down that road, we will have innumerable numbers of nations establishing their own standards of conduct in this area; and it will clearly be a very chaotic situation.

The CHAIRMAN. Then, what do we do, though, if you cannot get international agreement? It is clear that you are not going to get international agreement that wage differentials are an unfair practice. The countries that have low wages simply couldn't enter into it. I doubt if you are going to get them to agree that they have got to adopt our form of antitrust laws or that that is an unfair trade practice. Yet, what do we do in situations like copyright pirating or like inability to get into the services area in Korea? I know we have filed 301 cases. In essence, we are there unilaterally saying that those are unfair trade practices.

Ambassador YEUTTER. That is correct.

The CHAIRMAN. Now, where do we draw the line for ourselves on ourselves?

Ambassador YEUTTER. It does seem to me, Mr. Chairman, that we have to protect our own interests in this country so that we are not being maltreated by other nations; and if we find it impossible to do so under the GATT, or whatever international mechanisms exist, then we have really three choices: the pluralateral route, the bilateral route, and the unilateral route.

The CHAIRMAN. There aren't many others. True.

Ambassador YEUTTER. Yes.

The CHAIRMAN. Senator Danforth.

Senator DANFORTH. Mr. Yeutter, I think the answer is that we draw the line by never drawing it. That is, the basic policy of our Government has been—hopefully it is different now under the new trade program—but the basic policy is that we don't retaliate under section 301, that we might file a case, but we don't retaliate. And we don't file all that many cases.

Ambassador YEUTTER. We have retaliated once since I have been here. That is the citrus case; and I would not be at all surprised if we retaliate some more and maybe, in some cases, very soon. I am told, Senator Danforth, that we have got demonstrations in Seoul today because there are some in Korea who feel that we are taking too harsh a stance with them on trade issues.

Senator DANFORTH. I think, in general, the question is about the administration's new stated approach to trade. That is, whether it is simply going to be stated or whether it is going to be a true policy. I don't think that section 301 is going to have any credibility if all we do is issue statements from the East Room of the White House about how we are going to use it, or if all we do is file cases without ever retaliating. We are going to have to retaliate. I wanted to say to you that this national trade estimate is something that has been very dear to the heart of Senator Bentsen; I think it was his idea. It was part of the 1984 Trade Act, and I think a very important addition to the 1984 Trade Act. I was very pleasantly surprised by it. I think that it is a good first edition of what I hope is going to be an annual event. I only have two comments on looking at it. One is that I would hope in the future, under the section "Estimated Impact," we could at least make a try at quantifying what the impact of barriers are on lost sales opportunities for the United States—just some effort to try to quantify it. And the second comment that I would have is that if you just thumb through these actions taken or proposal to be taken and look at them, it appears as though the actions are to talk about it. Again, the credibility of section 301 ultimately will lie on the ability to use it. If a referee blows his whistle and never walks off the yardage, pretty soon the game is going to deteriorate; and I think that that is what has happened.

Ambassador YEUTTER. I agree with that, Senator Danforth; and I also believe that we need to make sure we develop a process that will continually feed in new entrants to that list because I am sure, as you are, that there are a lot of unfair trade practices out there that just haven't been filtered into the Government.

Senator DANFORTH. Right. You don't want just a mountain of complaints that you never do anything about. The idea is key—notorious really—unfair trade practices that have a significant effect on trade. Then, what we are going to have to do is to fit in place a systematic approach to getting rid of them.

Ambassador YEUTTER. Yes.

Senator DANFORTH. And if we don't get rid of them, we have to retaliate at least on a selective basis, not retaliate against a hundred different practices all at once. No, and nobody is suggesting that. You are going to have to pick some in order to gain credibility.

Ambassador YEUTTER. I fully agree with that, Senator Danforth, because if we are just a paper tiger, nations will continue to procrastinate.

Senator DANFORTH. Back to the question of 201, and also your comments about the present state of GATT. I just made a futile effort on the floor of the Senate to oppose the textile bill. I thought it was a terrible bill, and I made the argument against it. I will tell you basically what the argument was. The basic argument was that the international trading system works, that it is worth preserving, that this is a blockbuster of a bill, that it deals with not simply one sector of the economy but with the basic trading system itself. It is a blockbuster. It affects that trading system. It attacks that trading system. The trading system is worth preserving: We make it work in the United States, and it can be utilized to the benefit of the American people. I further argued that, in addition to making the trading system work, there are remedies available to aggrieved industries short of specific quota legislation. And of course, those remedies—that remedy really—has been section 201 of the Trade Act. There has to be some way of deflecting the pressures that we are going to continually feel, and we saw them in this bill: textiles, shoes, copper, all lumped together. And there could be a parade of others: lumber, semiconductors, machine tools. It is unlimited; it goes on and on and on; and if we cannot deflect those pressures into something that is part of the system and say the system works and can take care of them, then the pressures will be unending, and they will be unbearable. A vote of 60 yesterday will grow to a vote of 70 a year from now when the trade deficit is well over $150 billion headed to $200 billion; and it is going to become unbearable. That is the problem with the administration's shoe decision. That is why we are going to have to, in my opinion, take some discretion away from the administration, although not totally; it is going to be a fine line. We had this debate, a sort of miniature debate, on the floor of the Senate yesterday. Senator Evans said don't take any discretion from the administration. Senator Cohen said that, in the amendment that I offered, too much discretion was given to the administration. It is a line; but I will say this right now: The perceived position of the administration is let them eat cake: Section 201 is not available, and you have opposed the extension of trade adjustment assistance. If an industry is in trouble, if it cannot compete, don't just phase it out: just let it drop—sink or swim—Darwinism. And that is not going to sell politically. It is not sustainable. If it is good Adam Smith economics—I mean, I don't think it is good economics—but if it is, if the people who wear the Adam Smith neckties around town think that this is just a wonderful idea, it may be to them; but they don't run for office. You don't see people who run for office wearing Adam Smith neckties. [Laughter.]

I mean, we have to take care of problems, manage problems; and we shouldn't be doing it all in Congress. We shouldn't be doing this in Congress; the administration should be doing it. But when the administration stonewalls, when its idea of trade policy is really trade doctrine, trade ideology, which is inflexible and unable to accommodate the pressures that we receive, then quota legislation will continue to come down the pike. So, what we are going to do is to try to hedge in the President's discretion. Now, you will oppose it. I know it is further veto bait. A lot of people will oppose it. Senator Packwood will oppose it. But the two options cannot be: rampant protectionism enforced by crazier and crazier legislation to come onto the floor of the Senate and the House, on one hand, and simple textbook ideology on the other hand. There is no future in that. There is no future in that. The Reverend Danforth has preached his sermon. [Laughter.]

Ambassador YEUTTER. If I may just respond for a few seconds on that, Senator Danforth, I really believe that is a misrepresentation of the administration's view—not a personal misrepresentation by you, but the perception that allegedly exists with respect to the rigidity and inflexibility of the administration is, in my judgment, in error. I really believe that there is greater flexibility and pragmatism there and not quite as much ideologically positioning on the far end of the spectrum as might be viewed in your comments, Senator Danforth. I hope that we are a little more realistic than that. And I really think that even the record on the administration of section 201 over the last 4½ years would belie that evaluation. I covered all that in my testimony today because I assumed that would be of interest to you.

The CHAIRMAN. You granted three out of five, as I recall.

Ambassador YEUTTER. Yes; and of all the cases that have come up, as I recall there were 11 cases—6 of them in which the U.S. ITC found no injury, and that left five in which injury findings were made. The only two rejections out of the five were footwear and—I have forgotten the other one now—copper. Yes, footwear and copper. In copper—and copper precedes me—there were very strong indications that there would be more jobs lost than gained in that one. So, it seems to me, Senator Danforth, that Section 201 has worked reasonably well over the last 4½ years. So, I would say the situation is not quite that bleak. The other comment I would make is that all of this together—all of us collectively as Government have to make a judgment call, at some point in time, as to how much we, the Government, should do and wish to do for industries that lose their international competitiveness. We could obviously preserve them all, preserve every job, no matter what the cost. That would be the other end of the spectrum. We could do that in a lot of ways, including shifting to the system that prevails in the Soviet Union and elsewhere; but I know you don't want to go that route and neither do I. So, the question is: Where on the spectrum do we go in terms of responding to the trevail of an industry that has lost its competitiveness? And there, it seems to me, there is a lot of room for argument and a lot of room for movement. You suggested that we are pretty hardhearted in that respect; and certainly, we believe in a market system and will always do so. We think that adds some vibrancy to the American economy, and we would like to preserve that. But at the same time, there may be a little more compassion available on this side of town than what has been mentioned.

Senator DANFORTH. I will tell you this. Among the politicians—you know, among the ones who are weighing how to vote on quota legislation—there is a very strong perception that section 201 is just a dead-end street. I believe industry feels that way also. And I think one of the measures would be how many section 201 cases are being filed. I will bet that you are not going to have too many others who will wade into the thicket that the shoe people got into. I would like to be convinced. I would say this. We are going to be wrestling with this. We are going to have some proposed legislation in the very near future, hopefully next week, dealing with a lot of things, including section 201 and its future. It seems to me that one of the tests that should be established for the willingness to provide section 201 relief is whether the industry is able to regroup and rebuild and set itself on a path that is heading somewhere. If it is just a matter of throwing a few matchsticks and toothpicks to somebody who is going under anyhow, that is one thing. On the other hand, if a plan can be created that offers some future for an industry, then I think that there should be a possibility—certainty really—of at least limited relief, at least for a 5-year period when you would say: take this plan which is believed to be workable, put it in place, and let's see what happens. Let's give you a chance to survive. Let's not just prematurely decide that you are not competitive, and let you go under without so much as waving you goodbye.

The CHAIRMAN. Now, I want to ask Jack a question. In that case, why have these industries not been able to adjust before? They can't be blind. They have seen the competition coming. It is not like all of a sudden they need 5 years. They have seen it coming from 1960 and 1965 and 1970, and we started with the multifiber agreement about 17 years ago or 15 years ago. Why are they unable to adjust?

Senator DANFORTH. Let me say that I think the situation in trade has changed very, very rapidly. You can see that in the numbers. Just in this decade, there has been a huge change in the trade deficit and very rapid changes that can affect certain industries and cause them to go under very, very quickly. You know, I think that there are some perpetual weaklings. I think that there are some industries that have really just been crying for a long time without trying to pull themselves together. That is the kind of thing that should be weighed in determining whether there is viability.

The CHAIRMAN. Didn't shoes get three years of relief under president Carter?

Senator DANFORTH. Shoes did, I think, and then it wasn't renewed.

Ambassador YEUTTER. And in adjustment assistance, it is really earlier than that now, all the way back to the Ford years. So, there was some kind of assistance from about 1976 or 1977 through to 1981, either adjustment assistance or the VRA's.

The CHAIRMAN. And these are low-wage industries by and large, or at least they are certainly not high-wage industries that we are talking about. You alluded to a couple of high-wage industries, one of which was steel, in which you said that the cost of labor was simply greater than the productivity. Let me ask that question in a slightly different way. In essence, are you saying that the American steel industry for a long period of time, and the United Steel Workers, did not really care what wages they paid so long as they all paid the same wages and there was no import competition?

Ambassador YEUTTER. That is precisely correct. There seemed to be no recognition of the international competitiveness of that industry until a very recent date. And as I put it, Senator Packwood, when someone discussed with me the closing of a plant not too long ago because the laborers in that particular plant did not want to reduce their wage demands, my comment there was that, as between $12 an hour and a 40-hour work week and $18 an hour and no work, I think I would rather have the $12 an hour and a 40-hour work week. At some point in time, those $25, $30, and $35 per hour wages get one in trouble.

The CHAIRMAN. I have not reread the testimony lately, but I remember when we first put into effect the automobile mileage standards after the 1973–1974 boycott, we were putting them into effect from the standpoint of energy conservation, strongly opposed by the auto industry for two reasons. Even though they had until 1985 to meet the 27.5 miles per gallon standard, one was that they couldn't make it by that time. They said from an engineering standpoint, they couldn't do it by that time. Clearly, they could. Two of the companies had some trouble. Now, that was not because they couldn't make it; the market didn't want to buy their cars right now. The other argument was that the public didn't want to buy cars like that, anyway, and this was taking the decision out of the marketplace. Now, this was not 1955 when the only foreign cars we had were a few Rolls Royces and funny-looking little bugs that were driven by funny-looking little people. [Laughter.]

The CHAIRMAN. This was 1975, and we already had lots of Volkswagen competition and a fair amount, at that stage, of Japanese competition; and the industry was still saying that the public didn't want those kind of cars. And then, by 1978, 1979, and now, they want domestic content. They want voluntary restraints. Are we to protect industries that make those kinds of mistakes when they just say that the marketplace doesn't want that? Do we give them 5 years to adjust from their own mismanagement?

Ambassador YEUTTER. It seems to me that that is a very critical question in this entire section 201 debate, Senator Packwood. I would answer it by saying the following. It does not seem to me unreasonable in a capitalistic economy with a market-oriented base to expect industries and firms to learn how to compete and survive. It seems to me that that has been the heart of this country's economic system for 200 years, and it has served us well. Therefore, it that be correct, then it is the exception that must be justified; and that is really the heart of section 201 in which the Government of the United States, the Congress, and the administration conclude that there are some exceptional cases, that there are instances in which the Government ought to help, where the adjustment just doesn't take place for some unique reason that merits the Government injecting itself into that capitalistic process and providing some help. But that should not be the routine case; it seems to me that that clearly should be the exception rather than the rule. My fear here is that we are contemplating moving toward making section 201 the rule rather than the exception; and that gets us a long way away from the kind of economic system we have know for 200 years.

The **Chairman**. Mr. Ambassador, I am going to excuse myself and go off to the conference that is starting on the Gramm-Rudman debt ceiling provision; and hopefully, if we adopt that, that will help the value of the dollar and make us more competitive. I am going to let Senator Danforth finish, and I thank you very much.

Ambassador **Yeutter**. Good luck.

The **Chairman**. Thank you.

Senator **Danforth**. I won't keep you long, except to say that, obviously, the question should not be one of always providing relief versus never providing relief. From the administration's vantage point, Congress is about to take the position that this should be the rule rather than the exception. From our vantage point, the administration is so tough on this issue that it is really the extreme exception and 201 amounts to nothing. I would make one observation to you. This is an international system we are in. Other countries provide import relief for troubled industries. Other countries target infant industries for special protection and coddling and for future openings into other countries' markets. Section 201 isn't some strange anomaly created by a bunch of oddballs in Congress. Section 201 is provided for under article 19 of GATT. If we are going to be competing with the rest of the world, it doesn't seem reasonable to me for us to be developing a rigid ideology, if that is what we are doing, while the rest of the world is most willing to be highly pragmatic and fostering whatever they want to in their own country.

Ambassador **Yeutter**. But, Senator Danforth, what I find hard to understand in this debate is how people here on Capitol Hill have come to the conclusion that the administration is inordinately rigid in this area when there have been only two section 201 rejections in 4 years and 8 months.

Senator **Danforth**. Clayton Yeutter, you and I have discussed this in my office, and you have agreed with me.

Ambassador **Yeutter**. Which part? [Laughter.]

Senator **Danforth**. That it is extremely difficult for any industry to get import relief from this administration.

Ambassador **Yeutter**. But not impossible. That is a very important point. I feel very strongly that—you know, I believe in a capitalistic system, and I believe in the desirability of competition. I spent a lot of years out there learning how to survive and survived pretty well; and I think that is what makes this country strong. I think the burden of persuasion should be very strong. It just seems to me that gives vitality to the system. I am going to give you an example—a contrast in Mexico. I have just been down there a couple of times recently and had discussions with their top economic officials. They have concluded, properly in my judgment, that they have been too soft on their own domestic industries. They have been too willing to give import relief. Therefore, their industries have not become internationally competitive. Someone said to me there—and I won't quote the source—that our problem is that we are not internationally competitive in anything, and we have not provided an environment that has fostered our own international competitiveness. It seems to me that we have got to be careful about that.

Senator **Danforth**. I am no protectionist. I am not advocating protectionism. I think that that is the road to nowhere. I don't think that we should go to the role of Mexico either. All I am saying is that there has to be a willingness on the part of the administration or on the part of the system itself to accommodate these pressures to provide at least some reasonable possibility that, if you have a viable industry, you can keep it going for a while.

Ambassador **Yeutter**. Import relief, as you know, Senator Danforth, was granted in three of those cases—three out of the five, that came to the President. Now, the burden of persuasion was high in all those cases, but it happened—and steel being the big one. That wasn't done through the 201 process, but essentially the same result was achieved. So, I think it is unreasonable to charge the administration with being inordinately rigid.

Senator **Danforth**. All right. We will have many chances to argue this point. Thank you, Mr. Ambassador.

Ambassador **Yeutter**. You bet.

[Whereupon, at 12:47 p.m., the hearing was adjourned.]

[The following communications were submitted for the record:]

OVERSIGHT HEARINGS ON U.S. TRADE POLICY
STATEMENT OF MITCHELL J. COOPER IN BEHALF OF THE FOOTWEAR DIVISION OF THE RUBBER MANUFACTURERS ASSOCIATION

The Rubber Manufacturers Association is the trade association which speaks for producers of most of the rubber-soled footwear with fabric uppers and waterproof footwear manufactured in this country.

Rubber footwear imports have gone from 33 million pairs in 1964 to 124 million in 1984. During this period domestic shipments have shrunk from approximately 178 million to 80 million pairs. In short, fabric-upper rubber-soled imports have increased from 15.2% of the market to 61.8% over the past twenty years, and waterproof imports have increased from 19.9% to 56.2% of the market over the past ten years (The Government did not collect figures for this segment of the industry prior to 1975). In the past ten years employment in this industry has been reduced by 50%. These developments have occurred despite the fact that rubber footwear duties are high and were not cut in either the Kennedy or Tokyo Round of GATT negotiations.

More than 90% of all rubber footwear imports come from three Far Eastern countries, Taiwan, Korea, and the People's Republic of China, where labor rates are so low that the relatively high duties applicable to rubber footwear have not been able to stem the tide of foreign competition.

I suggest that the time has come for the United States to address the question of whether labor conditions and wage rates prevailing in the Far East require a redefinition of what is "fair" and "unfair" trade. The vast disparity which exists in labor costs for this industry and its import competition has resulted in an erosion of domestic production which now threatens the survival of rubber footwear manufacturing in this country. Nor would the removal of foreign trade barriers or the restoration of the dollar's traditional value have a meaningful impact on this industry. We can no more hope to compete effectively with Taiwan, Korea and the People's Republic of China abroad than we can in our own market, and the currencies of Taiwan and Korea are tied to the United States dollar.

The United States must grapple with the question of whether it is in the national advantage to retain such state-of-the-art, labor-intensive manufacturing industries as rubber footwear. If the answer to this question is in the affirmative, it will be necessary to redefine concepts of fair trade so as to impose some kind of reasonable limit on the imports of such labor-intensive products until and unless there is a substantial narrowing of the existing gap in labor costs.

As a possible first step toward the resolution of this problem, we recommend that any new multilateral trade negotiation be preconditioned on the willingness of its participants to broaden the concept of subsidies so as to include a consideration of fair minimum labor standards.

STATEMENT OF HARRY FIRST
PROFESSOR OF LAW
NEW YORK UNIVERSITY SCHOOL OF LAW

on

DISTINGUISHING BETWEEN "FAIR" AND "UNFAIR" TRADE PRACTICES OF FOREIGN COUNTRIES

For Oversight Hearings on United States Trade Policy
Senate Committee on Finance

November 14, 20 and 21, 1985

Mr. Chairman and members of the Committee. I am submitting this Statement in the hope that I can assist the Committee in its effort to set an overall framework for United States trade policy. My area of specialization is antitrust law,[1] and over the past several years I have become increasingly concerned about the application of antitrust principles in an increasingly internationalized economy. In 1983-1984 I was a Fulbright Research Fellow in Japan and a Visiting Professor on the Faculty of Law of Sophia University in Tokyo. During that period I engaged in research on the content and enforcement of Japan's antitrust law; this study enabled me to gain a greater appreciation of how antitrust enforcement relates directly to US concerns over foreign trade and trade policy.

My research subsequently came to the attention of the American Natural Soda Ash Company ("ANSAC"), a Webb-Pomerene Association whose purpose is to enable US soda ash firms to compete more effectively abroad. ANSAC believes, as do I, that greater attention to the enforcement of foreign antitrust laws must be an important component of US trade policy. Accordingly, ANSAC requested that I prepare this Statement to elaborate on this view.

---

[1] A copy of my curriculum vita is attached.

My Statement is divided into three parts. In Part I, I discuss the importance of focusing on private unfair trade practices and the failure of foreign governments to invoke their own laws to stop these activities. In Part II, I suggest that US antitrust law offers some useful guidance in determining what practices should be considered "unfair." In Part III, I offer some tentative suggestions on how the United States might increase the enforcement of foreign antitrust law by foreign governments.

I

I begin with an often neglected point. Trade is carried out by business firms, not by governments. Although there is, in each country, a varying amount of governmental involvement with these firms, including, of course, outright ownership, this should not obscure the importance of examining the behavior of business firms as distinct from the behavior of government. Business firms around the world make numerous decisions which may have a significant impact on the ability of US firms to compete; these decisions can involve the purchasing of inputs, the pricing and distribution of outputs, mergers and consolidations, joint ventures, the acquistion and licensing of technology, the participation in industry groups which set standards or establish the "rules of trade."

In recent years our trade policy has been concerned with such activities mainly to the extent that we could connect them to government action. Indeed, the press release calling for these hearings requests comment on how to distinguish between "fair" and "unfair" trade in the context of a legislative focus "on the 'unfair' trade practices of foreign nations" (emphasis added). This focus leads us, first, to overestimate the importance of foreign government ministries in controlling trade; and, second, to underestimate the significance of collusive behavior by private firms, which can at times effectively control foreign markets to the detriment of US firms and all consumers. The result is a deflection of our trade policy. When ministries like Japan's Ministry of International Trade and Industry (MITI) bemoan their lack of power to control today's markets we are left with no remedy other than to disagree with their assessment and ascribe to government a power which it might not have.

This brings me to my second, and even more neglected, point. To say that the conduct of foreign private firms might be at least as significant a barrier to foreign trade as foreign government policy does not mean that government policy is irrelevant to private action. On the contrary, there is a very significant relation between government policy and private firm behavior,.but it is a relation we miss because it does not occur.

This is the failure of foreign governments to enforce their own antitrust-type laws, laws which, if enforced, could open markets to competition. Governmental willingness to allow cartels to, for example, exclude foreign competitors, or fix high resale prices, or jointly cut prices to gain control of an industry, is just as much government policy as any decision to grant the industry a subsidy or tariff protection. Indeed, the economic benefits to the private firms are precisely the same.

Our disinterest in foreign antitrust enforcement springs from a number of factors. For one, I think we underestimate how many governments have adopted antitrust provisions. Antitrust laws have been adopted by a majority of the twenty-four members of the Organization for Economic Cooperation and Development (OECD), a group which includes not only Western European countries, but Japan, Australia, and New Zealand. The European Community has a transnational antitrust law, established in the Treaty of Rome in 1957. Other members of the antitrust club include countries as diverse as Korea, Taiwan, Argentina, Brazil, and India.[2] Although many of these laws may have been adopted with US encouragement, we should not therefore assume that these antitrust laws must be legal orphans in their new foreign countries. The opposite, in fact, is true. Each country has placed its own stamp on its antitrust laws; in some countries, such as Japan, the legislatures have strengthened the original provisions. We thus need not feel embarrassed about urging these countries to enforce their own laws.

---

[2] Foreign antitrust legislation is described in 2 W. Fugate, Foreign Commerce and the Antitrust Laws 359-401 (3d ed. 1982).

Another reason for our disinterest is that we have lost sight of how the antitrust laws can be used for business. The growth in foreign antitrust legislation was in part a post-World War II phenomenon, responsive to the lessons learned at the time. We saw that the private cartel movement had been allied with the growth of totalitarianism;[3] and that cartels hurt not only consumers but also deprived businesspeople of economic autonomy.[4] These concerns have faded from our view. Today, US antitrust enforcement policy views antitrust as being more often harmful than helpful to the economy or to business firms.

Current devotion to a laissez-faire antitrust policy, however, assumes a relatively open economic system. Whatever the truth of that in the US, foreign economic systems are often not very open, particularly to outside competition. A case in point is the soda ash market in Japan. In 1983 Japan's Fair Trade Commission brought a proceeding against four Japanese firms which manufacture synthetic soda ash and import natural soda ash into Japan (the "Soda Ash Cartel case").[5] This was one of those rare cases in which Japan's government, after prodding from the US Embassy in Tokyo, took antitrust action against a cartel of Japanese competitors. This cartel had been restricting imports of natural soda ash for a decade. In the year following entry of the FTC's order, soda ash imports increased from 58,000 tons to 126,000 tons. This was testimony to the usefulness of foreign antitrust law enforcement to US business in opening markets--as well as the usefulness to Japanese consumers who were now able to buy the preferred product.

---

[3] See, e.g., G. Stocking & M. Watkins, Cartels or Competition? 286-89 (1948).

[4] This point is made with great force in E. Hadley, Antitrust in Japan (1970).

[5] The case is explored more fully in First, Japan's Antitrust Policy: Impact on Import Competition, in Fragile Interdependence: Economic Issues in the Japan-U.S. Relationship (T. Pugel & R. Hawkins, eds., forthcoming); a relevant excerpt from this paper is

The Soda Ash Cartel case is one of the few examples where we have forced a foreign government to alter its policy of weak antitrust enforcement and police the conduct of private firms. It is also an example of how it may be as difficult to get an uncooperative government to enforce its antitrust laws as it is to get it to change other government policies which protect markets and hinder competition. It turns out that the relief order the FTC entered in the case was distressingly inadequate. The United States Trade Representative's most recent National Trade Estimates Report shows that the US industry's share of the market will decline from 17 percent in 1984 to 15 percent in 1985, and the US government must once again ask Japan's FTC to enforce adequately its antitrust law in this area. Thus, the Soda Ash cartel case stands as continuing testimony to how the combination of clearly private cartel behavior can interact with

---

attached to this Statement, infra.

passive government enforcement, thereby creating an "unfair trade practice of a foreign nation."

II

We have spent nearly 100 years in the United States trying to distinguish "fair" and "unfair" trade practices, trying to decide what might be beyond the bounds of permissible competition. All too often in this debate the term "fair" has been a code word for protectionism. There were twenty-three volumes of Codes of "Fair Competition" adopted between 1933 and 1935 under the National Industrial Recovery Act, codes which reflected "the businessman's ethical principle that the price cutter is a 'chiseler.'"[6] The "Fair Trade" movement sought to relieve small retailers from price competition by allowing resale price fixing; this departure from normal antitrust principles lasted nearly 40 years.[7] Thus, the usual antitrust view is that what some sellers perceive as "unfair" competition is really only hard competition.

"Fairness" having been given a bad name, some would prefer to delete the concept from antitrust consideration. I would take a different view. I believe that our antitrust experience shows the importance of retaining some concept of "fairness" in the operation of our economic system; but this experience also suggests the limits of the concept. More to the point here, both lessons may usefully be applied on the international level, where the concept of "fairness" similarly is threatening to become a code word for protectionism.

---

[6] J. Dirlam & A. Kahn, Fair Competition: The Law and Economics of Antitrust Policy 5 (1954).

[7] The Miller-Tydings Act, passed in 1937, was repealed by the Consumer Goods Pricing Act of 1975.

1. We have not had notable success in formulating a generic definition of "fairness" in domestic antitrust legislation. When Congress enacted the Federal Trade Commission Act in 1914 it gave the FTC power to enjoin "unfair methods of competition," preferring this broad approach to specifically designating certain practices as illegal. Our experience indicates, however, that the FTC has stayed fairly close to business practices considered "anticompetitive" under traditional antitrust standards. Even when the Supreme Court affirmed the Commission's power to apply its mandate "like a court of equity" and consider "public values" beyond those of the antitrust laws, the Commission did not seize the opportunity.[8]

2. Rather than a broad generic approach to "fairness," we do better with a focus on fairness as it relates to specific practices in a system of marketplace competition. Of course, we still need some overall guidance for the concept of fairness. Dirlam and Kahn, in their book Fair Competition, suggest that "[f]air competition is supposed to promote efficiency, and it is hoped that rules of fairness will ensure the preservation of

---

[8] See FTC v. Sperry & Hutchinson Co., 405 U.S. 233, 244 (1972).

competition iteslf."[9] This guide thus encompasses two benchmarks for fairness--the promotion of efficiency and the maintenance of a competitive process. The rules we adopt for international competition should seek efficient outcomes through the competitive process. They should be directed at providing the opportunity for all sellers to reach the market, so that competition "on the merits" can occur and the most efficient producers succeed.[10]

3. Without providing a laundry list of every practice which US courts have found to be anticompetitive, I think that there are certain practices which have historically been condemned because they "deprive . . . rivals of a fair opportunity to compete."[11]

a. Boycotts -- where members of an industry try to exclude competitors by jointly refusing to deal with them or by jointly using their power to coerce others to refuse to deal with them;[12]

b. Exclusive Dealing -- where a significant percentage of a market is foreclosed to outside suppliers by virtue of long-term supply contracts,[13] or by virtue of ownership integration;[14]

---

[9] Dirlam & Kahn, supra, at 18.

[10] Compare, e.g., Northern Pac. Ry. v. United States, 356 U.S. 1, 6 (1958) (evil of tying is that "[c]ompetition on the merits with respect to the tied product is inevitably curbed").

[11] Brown Shoe Co. v. United States, 370 U.S. 294, 324 (1962).

[12] See, e.g., Montague & Co. v. Lowry, 1903 U.S. 307 (1904).

c. Tying and Reciprocal Dealing -- where sellers (tying) or buyers (reciprocity) condition sales or purchases on the acceptance of a less-desired additional product;[15]

d. Bottleneck and Monopolistic Refusals to Deal -- where a monopoly buyer or seller uses it market power in the monopolized segment of the market to adversely affect competition at a potentially competitive level;[16]

e. Predatory Attempts to Monopolize -- Where a monopoly seller, or group of sellers, attempt to exclude an equally efficient competitor from the market, with the intent thereafter to obtain monopoly profits.[17]

4. There are, of course, many governmental policies affecting trade which do not deal directly with opportunities to compete, but can give protected firms an advantage over US competitors; examples include tariffs, subsidies (whether through

---

[13] See, e.g., Standard Oil Co. of California v. United States, 337 U.S. 293 (1949) (exclusive dealing).

[14] See, e.g., Brown Shoe Co. v. United States, 370 U.S. 294 (1962) (vertical integration).

[15] See, e.g., Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 104 S. Ct. 1551 (1984) (tying); Betaseed, Inc. v. U.&I. Inc., 681 F.2d 1203 (9th Cir. 1982) (reciprocity).

[16] See, e.g., Otter Tail Power Co. v. United States, 410 U.S. 366 (1973).

[17] See, e.g., Borden, Inc. v. Federal Trade Comm'n, 674 F.2d 498 (6th Cir. 1982); R. Posner Antitrust Law: An Economic Perspective 188 (1976).

direct expenditures or indirectly through the tax system), access to technology, and government procurement. Whether these advantages are "unfair" often depends on the extent to which US firms receive similar advantages in US markets; this is the subject of much dispute, and our own practices often weaken our arguments against them in other countries. The antitrust view of fairness is not subject to a similar charge. All firms operating in the US are entitled to, and receive, these protections. Private cartels face severe restrictions if they attempt to exclude competitors from markets. Application of antitrust rules in foreign countries, under legislation similar to our own, can produce a fairer trading system in which we ask only the same opportunity to compete that we offer others here.

III

"Fair trade" is trade in markets where private firms are adequately policed by government to insure all the opportunity to compete. Fairness relates to the process of competition. It does not insure results.

Once we see the connection between private anticompetitive behavior and governmental policy which tolerates such behavior, several approaches suggest themselves. At a minimum, US trade negotiators must put antitrust enforcement on the agenda of trade talks. I am pleased to see that this is being done in Japan with regard to several specific issues. This approach should now be generalized by paying greater attention to private firm behavior in those countries whose markets have been difficult to penetrate.

The step after trade negotiations is trade legislation. Obviously, this presents difficult problems, both in assessing the adequacy of foreign antitrust enforcement in light of concerns over excessive intrusion into sovereign law enforcement prerogatives; and in deciding what US sanctions are appropriate. Proposals to include inadequate antitrust enforcement under Section 301 of the Trade Act of 1974 are certainly one possibility. Whatever the approach, however, care must be taken to write legislation directed at specific practices rather than a generalized directive that foreign countries enforce their antitrust laws. The core unfair competitive practices described above would be a good start, and would avoid the trap of condemning nothing while appearing to condemn all.

Concentrating attention on private cartels and foreign antitrust enforcement will not solve all unfair trade problems. Industries which find it difficult to compete -- whether because of unfavorable exchange rates, high labor costs, or inferior technology -- will not be helped by being given a fair opportunity to compete in foreign markets. This approach will help only those US firms whose products can be successful in foreign markets. These are our winners. We should give them all the help we can.

Attachment to Statement of Harry First

Submitted For Oversight Hearings on United States
Trade Policy
Senate Committee on Finance

November 14, 20 and 21, 1985

Japan's Antitrust Policy: Impact on Import Competition

By Harry First*

The thesis of this paper is that the failure of Japan's Fair Trade Commission to more vigorously enforce Japan's Antimonopoly Act has adversely affected the ability of imports to compete effectively in Japan. This policy of inaction is government policy. Just like tariffs or targetting, it deserves the attention of those interested in opening Japan's markets to U.S. firms as fully as U.S. markets are open to Japanese firms.

* * *

---

* Professor of Law, New York University School of Law. The author would like to thank Richard W. Rabinowitz, Esq., for his helpful comments on an earlier draft.

© 1985 by Harry First.

II

On March 11, 1983, the Fair Trade Commission issued a "Recommendation Decision" involving four firms which manufacture synthetic soda ash and import natural ash. Under the Antimonopoly Act, a Recommendation Decision is the minimal formal level of FTC procedure; it represents a "finding" by the FTC that the Act has been violated, but this finding is made prior to the initiation of any formal complaint or hearing. The decision sets out recommended appropriate remedial measures, along with the facts supporting the Commission's findings.

The FTC found that the four soda ash companies had violated Section 3 of the Antimonopoly Act, which prohibits unreasonable restraints of trade, that is, agreements which affect price or limit output. These are the facts according to the FTC: The four defendants are the only soda ash manufacturers in Japan. In 1973, following liberalization of soda ash imports, the defendants entered into a memorandum agreement to prevent "disorderly importation" of inexpensive natural soda ash. They established a joint venture, along with seven trading companies, to build and operate a silo facility to receive and store natural soda ash. They then agreed to import natural soda ash, appointing four of the trading companies to handle the actual import arrangements, and the other three to distribute the ash from the silo to the defendants. The silos were made available only for soda ash imported by the four defendants through the trading companies. Equal commissions were paid to each of the trading companies regardless of the actual amount of import and domestic sales. The silo company, with a 30,000 ton capacity, began operations in 1975.

Although the four defendants agreed on an initial allocation of imports among themselves, they also met each December to set the total imports for the following year. Further, the 1973 memorandum provided that in the event additional U.S. companies wished to export natural soda ash to Japan "as new entrants," the four defendants "would cope with the problem jointly." Such an event occurred in 1979. At that time the defendants caused an alteration in the import-distribution system, switching trading company assignments around so that two new entrants could be served by one of the trading companies which was currently acting as importer (and was part-owner of the silo company).

The Recommendation Decision required the defendants, inter alia, to end the agreement on import quantities, allocations, price, and distribution channels. They were also required to "not unreasonably restrict" usage of the silos. The defendants accepted the decision. Data provided by the FTC show that imports of soda ash went from approximately 58,000 tons in 1982 to 126,000 tons in 1983; another report predicted an additional 40% increase for 1984.[21]

On its face, the Soda Ash case demonstrates how a decision to require Japanese firms to follow Japanese law can aid foreign firms, giving them the opportunity to compete in Japan's markets that Japanese law is supposed to guarantee. If all the case showed, however, was a vigorous FTC policing an aberrant situation by knocking a few firms back into line, then the case would not deserve much examination. In fact, what this case shows is the timidity of antitrust enforcement. What it suggests is an unwillingness to really deal with restraints on import competition, restraints which go far beyond the soda ash agreement.

To see this point, we need to return to the beginning of the story. The memorandum was signed in 1973; the Recommendation Decision was not entered until 1983. What finally triggered FTC interest? It was not the use of its substantial investigative power. Rather, it was a complaint from the U.S. Embassy acting on complaints voiced by U.S. producers.

Next, we need to look at who was not charged--the trading companies. It is hard to avoid the conclusion that they were active co-conspirators. They were co-venturers in the silo company. They were importing soda ash on behalf of U.S. firms, and then selling it to the U.S. firms' competitors (all the defendants were manufacturers of synthetic soda ash). The importing trading companies accepted the import quota agreed upon by the four defendants. Each of the seven then split commissions equally without regard to individual sales, thereby diminishing incentive to increase the sales of any particular U.S. competitor. Finally, when new U.S. entrants appeared, the trading companies simply swapped clients rather than break the quota system.

Next, we need to examine the competition story set out in the FTC complaint. Why was the agreement among the four companies effective in restraining import competition? After all, the four were not the only consumers of natural soda ash; in fact, only two of them used soda ash in their manufacturing processes. Soda ash is used in a variety of industries--bottle and window glass, soap, crude oil refining. All these manufacturers were required to pay higher factor prices; presumably, they would have preferred the lower prices offered by U.S. importers. Why could not the U.S. firms have simply avoided the four defendants (and their trading companies) and dealt directly with these customers?

One explanation might be the silo facility.[22] Perhaps it was an "essential facility," access to which would be required to compete effectively. Although it seems likely that use of the facility would have made it easier for new firms to enter the Japanese markets, there is no indication either that seller-provided storage was a requirement for sucessful sales, or that it would have been impossible for importers to build their own storage facility.

The more likely explanation lies outside the story told in the FTC decision. Apparently, the defendants, producers of synthetic soda ash, theatened their customers with a future refusal to deal, telling them that they would not sell to those who now purchased from the importers, if import supply became unstable in the future. Without this threatened refusal to deal, the defendants could not have controlled the actions of their customers, whose normal business interests would have led them to seek cheaper supplies. These joint refusals to deal violate Section 19 of the Antimonopoly Act.[23] Failure to specifically charge the defendants on this ground, like the failure to charge the trading companies, weakens the impact of the decree. The defendants were left free to employ their most effective weapon against their competitors.

There is a final important gap in remedy. The 1977 amendment to the Antimonopoly Act made a surcharge mandatory under the following circumstance: Whenever a firm "effects an unreasonable restraint of trade . . . which pertains to the price of goods . . . or results in affecting the price of such goods . . . by curtailing the volume of supply. . . ." This, of course, is exactly what the FTC found in the Soda Ash case. But it did not impose the mandatory surcharge, nor did it explain its reasons for ignoring this statutory requirement.

Given all that the FTC did not do, it should not be surprising that complaints are again surfacing about the behavior of the soda ash companies. In the year following entry of the decree, Japanese newspaper reporters began telling the Commission of renewed threats by the defendants to refuse to deal with those who buy imports; the U.S.-Japan Trade Study Group made a similar report.[24] So far, however, the FTC has not done anything to deal with these allegations.

III

The Soda Ash case suggests the role which antitrust enforcement could play in assuring competitive access to Japan's markets. It also shows how, even in a case in which enforcement appears vigorous, enforcement is in fact far short of what the law would allow. Of course, often the FTC is not even this vigorous. It is prone to allow defendants to escape with a warning, as it did in its 1984 decision regarding an agreement among domestic synthetic rubber manufacturers to restrict imports of synthetic rubber from Taiwan.[25] Further, there is a strong belief in the business community in Japan that agreements to restrict imports, backed by threatened refusals to deal, are quite prevalent. The U.S.-Japan Trade Study Group Report states that "Japanese businessmen acknowledge that such pressure is fairly commonly applied by Japanese firms . . . ."[26] Published reports of this pressure have surfaced in the petrochemical, fertilizer, and caustic soda industries.[27] So far, the FTC has not acted.

As important as this kind of enforcement would be, however, concerted refusals to deal with low-priced imports is not the only area of weak enforcement which affects import competition. I would like to suggest several other areas in which a change in FTC behavior could have a procompetitive effect which could benefit the position of imports.

First is the Commission's failure to pay more attention to the market for legal services, especially with regard to foreign lawyers. At present, Japan's government has attempted to deflect U.S. criticism of Japan's refusal to allow U.S. lawyers to advise clients in Japan by taking the position that this question is one for the Japan Federation of Bar Associations, a private trade association of lawyers. As might be expected, the Federation has not embraced the principle of opening its markets to new competitors.

The problem of allowing foreign lawyers to "practice law" in Japan has become enmeshed in issues of reciprocity, in the debate over whether having more lawyers in Japan will have an adverse effect on Japanese society, and even in negotiations over trade frictions. Lost in this debate has been concern with competition policy. Near total exclusion of foreign lawyers and law firms not only adversely affects these sellers of legal services. Decrease in the number of competitors affects consumer choice. All lawyers' services are not a deadweight loss to society; despite the usual criticisms of lawyers, it should not be forgotten that they do act to facilitate economic transactions, and that they can be useful in assisting clients who wish to achieve their business objectives. If foreign lawyers are most likely to serve the submarket of international business clients, it may well be that an increase in supply and competition in this market will lead to an increased ability of these firms to engage in economic transactions in Japan, and to penetrate Japan's markets.

Whether new entrant law firms would assist the entry of new imports, or represent current competitors (whether Japanese or foreign) intent on blocking them, is not clear. What is clear, however, is that the FTC has not articulated the policies favoring competition in this area. Normal competitive analysis would at least be skeptical of cartel control over entry of competing lawyers; and would predict gains at least in the primary lawyers market.[28] The Federation of Bar Associations does not appear to have any legally granted antitrust immunity. An investigation of the Federation's behavior might at least prod the Federation to adopt a more procompetitive policy. Instead, the FTC has left the matter to the parties "for negotiation."

This leads to a broader category of economic policy areas in which the FTC could improve the access of foreign firms to Japan's markets. It could act as "advocate for competition" in those matters of economic policy which have been given to other Ministries. This role would represent a change from the FTC's current posture of being a ministry which directs business, whether through guidance or orders, to end anticompetitive behavior; but it would not be inconsistent with the Commission's willingness to study issues of market structure and economic behavior. The role of "advocate for competition" should not be narrowly conceived in terms of advocate for foreign competition; rather the FTC should pursue a mission of seeking to increase competition generally in Japan's economy in much the same way that the U.S. Department of Justice's Antitrust Division does. Pursuit of this affirmative role, of course, would include import competition. Indeed, in many areas, imports are the most likely potential entrants.

There are many recent examples of policy issues in which an active FTC role might affect the competitive position of imports. These examples include: legislative battles over the proper structure for a privatized NTT and Japan Tobacco and Salt Monopoly Corporation; foreign access to VAN systems; the entry of commercial banks and securities brokers into the trust banking business; the type and length of protection for computer software programs. These are significant economic issues over which the FTC does not have direct jurisdiction; but the FTC's institutional posture as an advocate for competition might lead others to pay more attention to the impact on competition of their decisions.

The Commission has occasionally taken such an approach,[29] but, unfortunately, rather than acting as advocate for competition, the Commission's usual approach has been to close ranks with other Ministries when foreign criticism arises relating to opportunities to compete. This approach is exemplified by the Commission's 1983 Report on "Trade Frictions," in which it found virtually no competitive problems which particularly face foreign firms. The FTC's approach was one of looking for discriminatory barriers, rather than asking more general questions relating to the degree of competition in the markets studied. The general approach of advocate for competition, however, would have uncovered competitive problems, whose solution could benefit foreign and domestic competitors.

Footnotes

21. See U.S.-Japan Trade Study Group, Progress Report: 1984, at 69 (1984).

22. The importance of the silo facility is developed in Rapp, infra.

23. Pursuant to section 19, which forbids "unfair trade practices," the FTC has designated sixteen types of practices which fall into this category. Designation 1 covers concerted horizontal refusals to deal "without proper justification." Designation 2 covers unilateral refusals to deal under circumstances which are "unjust." Designation 11 forbids "unjustly dealing" with another party on condition that the party "shall not deal with a competitor, thereby tending to reduce transaction opportunities" for the competitor. Although it is not clear the extent to which the FTC requires proof of anticompetitive impact in such refusals (judged, for example, by the market share of the firms threatening the refusal), it would appear that the Soda Ash cartel did have sufficient market power to adversely affect competition through its threatened refusal to deal.

24. See U.S.-Japan Trade Study Group, Progress Report: 1984, at 69.

25. See "Warning to Synthetic Rubber Manufacturers," FTC Press Release, July 25, 1984.

26. U.S.-Japan Trade Study Group, Progress Report: 1984, at 70.

27. Id. at 69. See also The Japan Law Letter, Jan. 1985, at 21 (reporting that Japanese petrochemical makers are considering an arrangement whereby they would handle sales and marketing in Japan of petrochemicals soon to be produced by Saudi Arabia); id., Nov. 1984, at 41-42 (reporting MITI backing for such an arrangement, despite problems of legality under Antimonopoly Act).

28. Note, in this regard, that restraints on entry and competition in the legal services market go far beyond restrictions on the ability of foreign lawyers to maintain offices in Tokyo. As one observer has noted, "The Japanese legal services industry is subject to a wide variety of severely anticompetitive restraints, of which the barriers to foreigners are only one segment--and an incidental one at that." Ramseyer, Rethinking Regulation in the Legal Services Industry: The Relevance and Irrelevance of Culture, at 8-9 (1985) (unpublished manuscript).

29. See The Japan Law Letter, Jan. 1985, at 16-17 (reporting FTC opposition to Ministry of Posts' announcement that it might require Class 1 telecommunications applicants to unify their facilities prior to authorization of service).

OVERSIGHT HEARINGS ON U.S. TRADE POLICY

WEDNESDAY, NOVEMBER 20, 1985

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The committee met, pursuant to notice, at 9:30 a.m. in room SD-215, Dirksen Senate Office Building, the Honorable Bob Packwood (chairman) presiding.

Present: Senators Packwood, Danforth, Chafee, Symms, Grassley, Long, Bentsen, Baucus, Bradley and Mitchell.

The CHAIRMAN. The hearing will come to order, please.

This morning is the second in the most recent series of hearings we are having on the subject generally of trade. We will have another in this series tomorrow. And then when Senator Danforth and the others introduce their trade bill, we will be planning some hearings early next year on that subject. But I think at last we are putting the issue in a focus that we've not seen before, or if we have seen we have not discussed it. And that is not so much the issue are we faced with unfair trade practices, but what does the United States do when we are faced with trade practices which at least in the past have not been determined to be unfair, and I speak principally of low-wage countries and a great wage differential between the United States in certain industries and other countries in the same industries.

I emphasize, again, I'm not talking here about the normal unfair trade practices. Some of those are defined. Certainly, dumping is one of them. Export subsidies are another. And the normal commercial world defines those as unfair trade practices.

The United States, if it wanted, could unilaterally define other practices as unfair, although if we start down that road of every country saying for itself which of the other competitors' practices are unfair, I'm assuming there would be some reciprocity involved in that, and other countries would start saying the same thing about some of our practices. But the more relevant issue, in my judgment, is can the United States, can the bulk of its industries, compete against similar industries in other countries where there is widely disparite wage differentials. And if we cannot compete, say for those industries that we designate as critical to the national defense and we simply say we are going to save them no matter what, if we cannot compete, should we save those industries or should we let them go.

And the special trade representative, Ambassador Yeutter, the other day in response to that question said there are some indus-

57-470 O - 86 - 4

tries that we just ought to face up to it and let go that are not critical to the national defense.

And, of course, that last issue is a difficult one to face because I've yet to find an industry when they testify that don't honesty feel that are critical to the national defense. It does not matter what industry it is. In their minds, the national defense depends upon their continued existence in this country.

I know the witnesses have been asked to address themselves to that. I've had a chance to read the testimony, at least of the testimony that was in as of 5:00 or 6:00 last night. Most of the witnesses have. And I think by the time we are done with these hearings and the hearings on the Danforth trade bill, we are going to have a record as to whether or not the United States can compete against low- wage differentials; whether or not we should compete in all industries against low-wage differentials.

Senator Long.

Senator LONG. No questions at this point, Mr. Chairman.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. No questions, Mr. Chairman.

The CHAIRMAN. We will start this morning with a panel of two of the brighter lights in my estimation in the field of labor and the field of trade: the Honorable Paula Stern, who is the Chair of the International Trade Commission; and the Honorable Janet Norwood, who is the Commissioner of Labor Statistics for the Department of Labor. And unless either of you have any objections, we will take you in the order that you appear on the witness list, and take Chairwoman Stern first; ask you to abbreviate your remarks as much as possible, and give us a chance for questions.

Ms. Stern.

STATEMENT OF THE HONORABLE PAULA STERN, CHAIRWOMAN, INTERNATIONAL TRADE COMMISSION, WASHINGTON, DC

Dr. STERN. Thank you very much, Mr. Chairman, for the opportunity to present my views on U.S. policies toward our trade problems. In my 7 years at the ITC, I've had many opportunities to observe how U.S. businesses fare against both fair and unfair international competition, and how our policy apparatus affects our international competitiveness both by acts of omission and commission.

I'd like to make three basic points. First, the job of enforcing our Nation's trade laws is important. We can't afford complacency in the face of unfair practices by our competitors. The current trade crisis has seen an explosive growth in unfair trade bases under the countervailing duty and antidumping law and section 337 of the Tariff Act of 1937. With rapidly growing imports steering our trade deficit toward $150 billion this year, it's no wonder that American producers are especially sensitive to the unfair practices.

An individual industry doesn't have much control over U.S. economic policy, but it can file a case at my agency, and that's as it should be.

My second point is that our Nation's enormous trade problems can't be solved by actions in the unfair trade area alone. Since I came to the ITC, I figure I've voted on about a thousand or more investigations so I think I can offer some perspective. In general, the Commission finds grounds for action in the unfair area in only a little over 50 percent of the cases we examine.

Last year, in fact, less than 5 percent of the total value of U.S. imports coming into this country was even challenged before the ITC.

During 1985, we've seen so far only about 1 percent of the imports has been challenged.

In the vast majority of the cases we probe, an affirmative Commission ruling only results in marginally raising the price of imports, not——

The CHAIRMAN. Let me interrupt. Challenged at all, or the challenge is unfair? Or do you mean even challenged under——

Dr. STERN. Challenged as unfair under the section 337 and under our title VII dealing with dumping and subsidies.

The CHAIRMAN. OK.

Dr. STERN. These are the unfair cases.

And in most of those cases, we can only raise the price of those imports. We can't eliminate them from the market.

To be sure, my figures do understate the problem by looking just at the unfair practices in imports in our home market, not overseas. But there is an underlying reality to this. To remedy our disastrous trade deficit, we will have to look beyond the ways in which foreigners close their markets and abuse our hospitality at home. And this brings me to my third and final point.

We need a major change in viewpoint when we write our laws and set our policies. Until the 1970's, our relatively self-sufficient Nation did very well treating trade as a secondary situation. But those days are gone for good.

National economic legislation and executive action must become trade oriented. We simply can't afford policies which treat the trade sectors of our economy as stepchildren. Trade effects must be factored in from the beginning.

Since the end of 1983, I figure I've been speaking about the connection between the budget and the trade deficits. The missing link between the budget and the trade deficits is the bloated dollar. It has played havoc with American industry, mining, and agriculture. Fortunately, the administration stopped touting the dollar, the strong dollar, and it has begun to treat it as one of the prime causes of our trading weakness.

But even with coordinated exchange rate intervention, as we see it, it will take a lot more than just talk to get the dollar down. We simply must change our Nation's buy-now, pay-later ways. They don't sit well in a world of tough save-now, buy-later competitors. And it will take hard work to recapture the customers that we have lost from our rivals.

All of us have heard quite a bit on this subject. We all hope for aggressive action to straighten out both remaining unfair practices and our odd macropolicy mix. But there are also some excellent things that I think can be done so that U.S. firms can compete in the hoped-for world of fair trade and a lower dollar, because ultimately the tilt of the playing field is not going to determine who wins this fray. It's going to be how tough we are as competitors out there on that field.

I think that our best creative energies should be concentrated, therefore, on rebuilding the strength of the American team. In section 201, import relief cases, Congress could provide the ITC with directions to broaden our analysis when these industries come in, and when appropriate, the ITC, then, could recommend more comprehensive remedies. I also believe it would be wise to establish an auction for quotas in order to finance adjustment packages for firms and for workers.

I think we should continue our concern with unfair practices, but even if we succeed in making the world safe for American trade, we must remember that our primary concern ought to be the competitiveness of our industries, services, farms, and mines. Competitiveness can be encouraged if we start approaching both the policy and the legislation with a much more trade-oriented approach.

Thank you.

The CHAIRMAN. Thank you.

[The written statement of Dr. Stern follows:]

DR. PAULA STERN, CHAIRWOMAN
U.S. INTERNATIONAL TRADE COMMISSION

Mr. Chairman, thank you for the opportunity to present my views on U.S. policy toward fair and unfair trade. In my seven years at the ITC, I've had many opportunities to observe how U.S. businesses fare against both types of competition.

As you know, the Commission administers laws under which American industries can obtain relief from both fair and unfair trade. Section 201 of the Trade Act of 1974, otherwise known as the escape clause, is the vehicle for relief from fairly traded imports. The antidumping and countervailing duty laws and section 337 of the Tariff Act of 1930 offer relief from unfairly traded imports. In my comments today I will be speaking for myself and not for the Commission.

The fairly steady post-war expansion in the volume of global merchandise trade came nearly to a halt between 1980 and 1983. Growth resumed last year, but much of the rise was due to the record-setting purchases of foreign goods Americans borrowed to buy.

The deterioration of U.S. trade performance since 1980 has been well-documented. Not only have we broken records, we broke what were supposed to be economic laws. During our own recession, imports grew even though domestic demand declined. That pattern defied history and expectation.

During our recovery, our appetite for imports swelled, but our export sales did not. Exports earned us $218 billion last year, only two billion dollars more than in 1980. The gap between imports and exports was $123 billion last year and may widen to $150 billion this year.

Causes of Declining Trade Performance

Explaining recent trade figures is difficult but essential if we are to develop sound economic policies. The most powerful force in determining America's laggard competitive performance in recent years has been the increase in the value of the dollar against other world trading currencies. We brought it on ourselves and, by doing so, gave our trading partners and rivals a competitive advantage at America's expense.

The ITC, after studying the agricultural sector, concluded a few months ago that up to 88 percent of the drop in U.S. farm exports between 1981 and 1982 was due to the rise in the dollar's value. And Federal Reserve Board experts blame the high dollar for 87 percent of the increase in our total trade deficit between 1980 and 1984.

You may take your choice of statistics, but the point is clear: the dollar has done great damage to America's trading position. Fortunately, the Administration has stopped touting the strong dollar and has begun to treat it as a prime cause of our trading weakness.

Almost two months have passed since that change of emphasis brought new policies into effect. But even though the dollar is still only 3-4 percent below its 1984 level, we should be encouraged by the shift and by the parallel efforts to generate new growth in both the industrialized and debtor nations.

Even with a significant, continuing drop in the dollar, we will not easily or painlessly recoup the jobs we have lost at home and the sales we have missed abroad. A steady decline in the dollar's value will, of course, eventually bring exports up and imports down.

It will be hard work to recapture customer loyalties here and abroad from new, determined and diverse rivals. And as a weaker dollar reduces competition from cheaper imports in our own market, inflationary pressures are bound to gain steam.

This forecast assumes, moreover, that the Administration's altered policies succeed. But we must recognize that the buy-now, pay-later practices which drove the dollar up are still at work.

American exporters have also been plagued by the debt problems of many developing countries. The shrinkage in Third World markets has been bad for them and bad for us. In Latin America alone, our regional trade went from a slight surplus in 1980 to a deficit last year of nearly $16 billion.

U.S. industry is also facing more fundamental competitiveness problems that have been masked by the recent shift in the dollar and the debt crisis. Low-wage competition, particularly from southeast Asian countries, has hit a broad section of U.S. manufacturers hard. Inadequate investment and management practices have also hurt American competitiveness.

Our trade relations with Japan illustrate this point. From 1981 to 1984, measured in dollars, unit labor costs in Japan declined by 15%, while in the U.S. unit labor costs rose by 6%. Thus, even a further fall in the dollar and removal of export barriers in Japan are still likely to leave us with a continuing problem in our ability to compete with Japanese businesses, either here or in Japan.

Unfair Trade Practices

I would now like to turn to major topic in the current political debate on trade policy: the impact of unfair trade practices on recent U.S. trade performance. The law-breakers in the global marketplace are numerous and imaginative. But the unfair trade practices of other nations, however vexing to individual U.S. industries, are not the chief menace to the trading system or to America.

On this point, I speak with the experience that comes from casting some one thousand votes on import relief cases of all sizes and shapes -- fair and unfair.

In the 1985 fiscal year that just ended, the ITC initiated 22 percent more investigations than in 1984, more than half again as many as in fiscal 1980. But as a rule, we find grounds for action in just a little over 50 percent of the cases we examine. In this we follow U.S. trade laws and the GATT which make clear that dumping and subsidization of imports are unfair and hence dutiable only if shown to materially injure a U.S. industry.

Last year in fact, less than five percent of U.S. imports were even challenged before the ITC. In the vast majority of those cases, an affirmative Commission ruling would only have resulted in marginally raising the price of imports, not in eliminating them.

Between 1982 and 1984 we levied countervailing or anti-dumping duties on barely $3 billion of U.S. imports. To be sure, this figure understates the problem. And there are other abuses which we still cannot measure in precise dollar terms -- a vast array of stratagems which work to bar our products and services from foreign markets.

These non-tariff barriers -- whether they are the picayune technical inspections or the chauvinistic government purchasing rules followed by Japan, among others -- are the nemesis of the open trading regime that is essential for growth. We must fight to remove those obstacles and fight hard.

But, to explain the $150-billion trade deficit facing us this year, we have to look beyond the ways in which foreigners close their markets and abuse the open hospitality of ours.

Our chief concern need not be the tilt of the playing field. We must concentrate instead on building the strength of the American team.

U.S. Competitiveness and Import Relief

If most of the trade we compete against is fair, how should we deal with it?

Many laws offer U.S. claimants relief from the strain of trade competition. But the approach that focuses narrowly on imports often overlooks more basic causes of competitive decline.

In "escape clause" cases where the ITC finds that imports threaten or actually cause serious injury to American industries, we are supposed to be able to recommend tariffs, adjustment assistance and/or quotas as relief. But there is now really only one item on our remedy list: quota restrictions on imports.

Tariffs, for instance, have not worked in an environment where an increase in the dollar's value swamps the effect of the added duty. Nor have we made good on promises to workers dislocated by import competition. The Trade Adjustment Assistance Act is due to expire soon, and the aid it has supplied often failed to identify new jobs or provide new, marketable skills. No wonder workers regarded it as little more than "burial benefits" for the unemployed.

Consequently, we are often left with quotas as the only available remedy. And when the President, on our recommendation or on his own initiative, selects such a course, that action alone accomplishes precious little to make the intended beneficiaries more competitive.

Consider for example, the Administration's five-year program to limit steel imports. If it reaches its current goal, the cost to U.S. consumers would be three quarters of a billion dollars in the first year of operation. And it may even harm us as exporters.

At the request of this Committee, the ITC is now examining how such restrictions would raise the cost of our manufactured exports and thus reduce our competitiveness. It will be interesting to find if we are robbing Peter to pay Paul. But we should have weighed those costs before, not after, we began negotiating the restraints.

At the same time, relief by itself is rarely the answer to competitiveness problems. In its present form it does not provide strong incentives for recipient industries to adjust to competition.

Unlike the Chrysler loan guarantees, there are no established performance tests setting conditions for granting or extending trade relief.

We could -- and should -- change this pattern by changing our definition of government's role in boosting American trade performance. Intervention must serve strategic goals, not simply respond to temporary distress or political clout.

Measuring the impact of imports alone neither tells us what the problem is nor directs us toward comprehensive solutions. And import relief is not now tied to private efforts to meet the challenge of international competition.

When the ITC now recommends relief, we give the President only a take-it-or-leave it option. We should offer a broad and deep range of choices based on an industry's competitive position and its readiness to adapt to new conditions.

I do not propose a vast, new government agency to oversee this work. The ITC already has the impartial expertise to assess the strengths and weaknesses, the prospects and problems of the industries which petition us for help.

We already see many situations where imports are only the symptom, not the chief cause, of a competitive problem. But our mandate does not enable us to suggest remedies to deal with problems inside an industry, only with threats that originate abroad.

We could be more useful if we could match the breadth of our recommendations to the depth of our investigations. Our analysis could serve in the future, as it has not in the past, to help government and business cooperate in setting common goals and a course toward them.

I would not, however, change the role of private initiative in triggering a government response. The first move toward cooperation should come, as now, as a form of petition -- but for revitalization, not just relief.

In exchange for trade or regulatory relief, for tax breaks or anti-trust law exemptions, industries should spell out their planned investments in modernizing production methods and equipment. Or in return for funding research and development or for long-term government procurement contracts, we might expect undertakings to pioneer new technologies.

Labor must be part of these strategic bargains. Where adjustment means contraction in the workforce and changes in work rules and wage structure, workers have to be participants in the process, not its victims. Government can cushion some of the pain with inducements to early retirement, but it should focus its efforts on positive measures.

Too many American workers, especially, in import-battered sectors lack the high school diplomas they need to advance into jobs with better prospects. Others can benefit most from job search and training programs that will help workers relocate and reequip themselves with up-to-date skills.

And expensive though this effort may appear, we could finance much of it without raising taxes or the deficit. Instead of simply giving away import quotas to Japan, Korea and other nations, we should be auctioning them.

We have ignored this possibility too long. For example, by allowing foreign producers to capture the quota profits, American import relief programs have helped finance the retooling of our strongest international competitors.

The voluntary restraint agreements in effect from 1980 through 1984 brought U.S. automakers some $9 billion in added revenues. But a recent ITC study shows that Japan earned an extra $5 billion as well. We can be more frugal and more creative.

The ITC, in fact, proposed auctioning quota rights as part of the relief it recommended last July for the footwear industry. The idea died, however, when the President rejected our entire package, and the question of how to administer such an auctioning system remains an open one.

More recently, two noted economists have estimated that an auction of quota rights in 16 fields where import levels are already assigned free of charge might net over $6 billion from foreign bidders in 1986.

That sum could represent significant seed money to plow back into honing our competitive edge. It could be a very succulent carrot to induce management and labor along with suppliers, creditors, stockholders and state and local governments to participate in workable revitalization plans.

Some will say that this sounds like more government intervention. But this proposal only recognizes the ineffectiveness of costly government intervention which is already taking place already.

All government decisions -- whether on taxation or investment, regulation or education, guns or butter -- play a part in forming or deforming our competitive posture. Import relief is no different.

But starting with the macroeconomic policies which I stressed earlier, we must make all our choices with full attention to their impact on our competitiveness.

Table 1.--Estimated value of U.S. imports covered by ITC cases from countries subject to the investigation, by investigation type, FY 82-85

Case type and fiscal year of initiation	Estimated U.S. imports covered by cases (calendar year data)	Percent of total U.S. imports 1/
	--Million dollars---	
Unfair trade cases:		
Antidumping:		
FY 82	3,390	1.4
FY 83	1,180	0.5
FY 84	10,150	3.1
FY 85	2/ 1,420	0.6
Countervailing:		
FY 82	6,390	2.6
FY 83	7,920	3.1
FY 84	4,310	1.3
FY 85	2/ 1,360	0.5
Section 337:		
FY 82	1,280	0.5
FY 83	1,610	0.6
FY 84	510	0.2
FY 85	2/ 3/ 60	4/
Total unfair practices (Antidumping, countervailing, and 337): 5/		
FY 82	11,050	4.6
FY 83	10,700	4.2
FY 84	14,970	4.6
FY 85	2/ 2,840	1.1
Other:		
Section 201:		
FY 82	240	0.1
FY 83	300	0.1
FY 84	15,300	4.7
FY 85	2/ 4,240	1.7
Section 406:		
FY 82	34	4/
FY 83	-	-
FY 84	1	4/
FY 85	-	-

1/ Total U.S. imports by year (million dollars):
1982--- $242,340
1983--- $256,680
1984--- $322,990
1985--- $254,800 (Jan.-Sept.)

2/ Trade data provided are for Jan.-Sept. 1985 only.

3/ Understated due to lack of trade data on many of the section 337 cases.

4/ Less than 0.1 percent.

5/ Trade shown under "Total unfair practices" is overstated due to instances in which identical products were investigated in both antidumping and countervailing cases.

Note: It is estimated that during Jan.-Sept. 1985 there were approximately $3.2 billion in U.S. imports under tariff items subject to outstanding dumping/countervailing duties. This is equivalent to roughly 1.2 percent of total U.S. imports during the period.

Table 2.--Disposition of FY 85 cases and the value of imports covered by affirmative/pending ITC investigations, by investigation type

Case type	FY 85 case numbers				Import value for affirmative/ pending cases 1/	Percent of total U.S. imports
	Total	Affirmative	Negative/ withdrawn	Pending		
					--Million dollars---	
Antidumping	82	4	40	38	$720	0.3
Countervailing	38	4	22	12	$490	0.2
Section 337	23	-	13	10	-	-
Section 201	4	1	1	2	$4,240	1.7

1/ Note that all cases initiated in FY 85 have not yet been decided. Trade data presented are for Jan.-Sept. 1985.

The CHAIRMAN. Commissioner Norwood—and I might say before she starts I have used your—I don't mean yours personally, but the Bureau of Labor Statistics—statistics over the years and found them almost without fail to be impeccably accurate. Unfortunately, in some cases because they weren't necessarily supporting conclusions I had come to. And I congratulate you on the strictness with which you have hued to a straight and narrow path regardless of where the chips may fall.

Dr. NORWOOD. Thank you.

STATEMENT OF HON. JANET L. NORWOOD, COMMISSIONER OF LABOR STATISTICS, U.S. DEPARTMENT OF LABOR, WASHINGTON, DC

The CHAIRMAN. Go right ahead.

Dr. NORWOOD. I'm very pleased to have the opportunity to talk to you a bit about some of our data, particularly on employment and productivity.

As you all know, over the entire post-World War II period, most of the employment growth in the United States has been in the service-producing sector. Currently, 7 in every 10 workers in this country are employed in the service-producing sector.

In the goods-producing sector, manufacturing is the largest component. And it, of course, is the most important in terms of trade.

While manufacturing has gained an additional 4 million jobs since 1950, this growth was dwarfed by the 47 million new jobs added to the service-producing sector. Even though the absolute number of factory jobs has increased since 1960, it is still below the 1979 level. And there have been a lot of job changes within manufacturing. We've had a number of industries, which I've described in my statement, which have gained jobs since the 1982 recession. During this recovery period, some have regained all and more than the number they lost. Some have not. And some have continued to lose jobs during the recovery period.

Of the six industries which continued to lose jobs, all but chemicals reached its highest level more than three decades ago, and current developments continue the long-term downward trend.

Now there are a lot of people in the country who fear that we are losing good jobs and gaining bad jobs. I think it is true that we've lost both high-wage and low-wage jobs in manufacturing, and we have gained a large number of jobs in services. But the widely held notion that all jobs in the service-producing sector are bad jobs is just not true. That sector, for example, employs 80 percent of America's managerial and professional specialty workers.

The fact is that the service-producing sector is extremely diverse, and we cannot categorize the jobs in it as being either low or high wage. We've got people working in fast-food restaurants, in rather low-paid jobs. But this sector is also the home of computer services, legal services, advertising and communications where workers on average earn fairly high wages.

BLS is in the process of releasing—we just had a press release releasing a new set of projections of the future. Those projections show that approximately 90 percent of the projected job growth to 1995 will continue to be in the service-producing sector.

We do expect factory jobs to increase, but probably not to the overall level which they reached in the late 1970's. So restructuring within manufacturing is expected to continue. Indeed, the nondurable part of factory employment is projected to decline. And within the service-producing sector, there will be some concentration of job growth.

I think one important issue that we have to remember is that employment losses in manufacturing are not always translated into losses in factory output. Real output data used in the BLS projections work show, for example, that over the last 15 years or so when a number of the nation's factories were losing employment, the real output of our manufacturing industry actually increased. And although we are projecting very small gains in manufacturing employment through 1995, we do expect factory real output to increase.

It's really the share of manufacturing as a part of the total that has declined, and that we believe will continue to decline.

Now I think it's important to look at developments in productivity because if wages and, therefore, workers' incomes are higher in the United States than abroad, we can still remain price competitive if we maintain an equal or greater productivity differential.

At the total economy level, the United States does remain the most efficient country in the world, as measured by gross domestic product per employed person. On the other hand, it is true that most other industrial countries have had much faster rates of productivity growth. The gap, therefore, has narrowed.

Now in looking at trade issues, it is much more important, I think, to look at manufacturing productivity. The available evidence there indicates that the United States still has the highest average level of manufacturing productivity, although I cannot state with confidence how large that differential may be. But this is no longer true for some manufacturing industries or products.

Now we have had a slower rise in manufacturing productivity than any of the other countries for which we have data. And they are all experiencing slow-downs, but most of them, like the United States, have improved in the last two years of recovery. Only a few, however, have surpassed their pre-1973 rates of gain since 1982.

Nonetheless, with the exception of Canada, all of the foreign countries continue to have faster average rates of manufacturing productivity growth than the United States from 1973 forward, with Japan continuing to lead the way.

Those changes in manufacturing productivity were accompanied by changes in employment. In the United States, manufacturing productivity did not maintain its pre-1973 rate of increase. Some other countries—Canada and Japan—have had jobs in manufacturing leveling off.

But while European productivity growth rates continued to surpass the U.S. average rate of gains since 1973, an important part of their superior productivity performance was accompanied by employment and hours declines. Now productivity growth rates for the United States have lagged behind those of our competitors, it is true, but it should be kept in mind that part of that differential reflects a catching-up process.

Comparative rates of productivity growth between the United States and countries approaching the U.S. overall level of efficiency should presumably narrow. However, this is not a certainty. There are many other factors that also affect relative rates of productivity gain.

I'd be glad to try to answer any questions.

[The prepared written statement of Dr. Norwood follows:]

STATEMENT OF
DR. JANET L. NORWOOD
COMMISSIONER
BUREAU OF LABOR STATISTICS
BEFORE THE
FINANCE COMMITTEE
UNITED STATES SENATE

November 20, 1985

Mr. Chairman and Members of the Committee:

I appreciate the opportunity to be here this morning to review with you Bureau of Labor Statistics data on current and projected employment trends in the United States. I would also like to touch briefly on productivity developments both here and abroad, because they are so important in evaluating competitiveness.

THE CHANGING INDUSTRIAL STRUCTURE IN THE UNITED STATES

Over the entire post-World War II period, most of the employment growth in the United States has been concentrated in the service-producing sector of the economy. In addition to the services industry itself, this sector includes retail and wholesale trade; transportation and public utilities; finance, insurance and real estate; and government. Currently, 7 out of every 10 workers in the United States have service-producing jobs, and there is every evidence that the service sector will continue to play a major role in providing jobs in the future.

This changing industrial structure reflects a leveling off of employment growth in the goods-producing sector. In 1984, employment in the nonagricultural goods-producing sector averaged just under 25 million, about the same level as a decade earlier. But since 1973 we have experienced three business cycles which created sharp upward and downward swings in goods-producing employment.

Manufacturing is the largest component of the goods-producing sector, and its 15.2 million jobs in 1950 accounted for one-third of all nonfarm jobs. While manufacturing gained an additional 4 million jobs in the ensuing 35 years, this growth was dwarfed by the 47 million new jobs added to the service-producing sector. Even though the absolute number of factory jobs has increased since 1950, it is still below the 1979 level.

Within manufacturing, job changes have been, and I believe will continue to be, very uneven. Over the three years of the current recovery, five manufacturing industries--lumber and wood products, furniture and fixtures, electrical and electronic equipment, transportation equipment, and rubber and plastics--have regained far more jobs than the number lost during the 1981-82 recession. Several others have increased employment, though not to the extent that they had lost jobs during the recession. The largest decreases, however, occur among those industries that have continued to lose jobs during the recovery period--primary metals, tobacco, textiles, chemicals, petroleum and coal products, and leather products. Of these six, employment in all but chemicals reached its highest level more than three decades ago, and current developments continue the long-term downward trend.

GOOD JOBS AND BAD JOBS

Many people fear that the structural changes I have been describing are causing us to lose jobs in the highly paid manufacturing industries and to gain jobs in the low-paid service-producing industries. What is often forgotten is that while we have lost some jobs in the highly paid manufacturing industries, we have also lost jobs in such low-paying industries as textiles, apparel, and leather manufacturing. Textile employment, for example, actually peaked in 1941; since 1973, the industry has lost almost one-third of its work force. On average, textile, apparel, and leather workers have the lowest earnings of all manufacturing industries.

I do not mean to minimize the problems of such high-paying manufacturing industries as steel and autos. The steel industry lost one-third of its jobs in the last recession and has continued to lose ground in the current recovery. But the decline in the steel industry began long before the recent recession. Lighter, stronger, and less costly products have been developed to replace steel, and, even where steel continues to be used, it is often rolled thinner, requiring less of the product to be used. Productivity improvements have occurred in the United States, and competition from efficient new plants abroad has increased. All of these factors have contributed to the secular employment decline for the industry.

The situation in autos is quite different from steel. Auto employment has shown considerable strength in the current recovery. More jobs have been added since the end of 1982 than were lost during the last recession. In spite of this strong growth, however, the overall number of jobs in the industry is still considerably below the level of 1979. Smaller, more fuel-efficient cars, many supplied by imports, were developed. Demographic changes have reduced the potential market for new cars, a large number of families already own one or two automobiles, and the increased cost of car ownership and operation suggests that Americans will tend to replace their automobiles less frequently than they did in the past.

We have lost both high-paid and low-paid jobs in manufacturing, and we have gained a large number of jobs in services. The widely held notion that all jobs in the service-producing sector are bad is just not true. The sector employs 80 percent of America's managerial and professional specialty workers.

The fact is that the service-producing sector is so diverse that the jobs in it cannot be categorized as either high-wage or low-wage. Many very low-wage workers are employed in the service sector--in fast-food restaurants, in personal service establishments, or in nursing homes. But this sector is also the home of computer services, legal services, advertising and communications, where workers, on average, earn fairly high wages. And we must also remember that the occupational composition of jobs in the United States is also shifting markedly. We need more research to determine exactly how the occupational and industrial restructuring that has been taking place affects the prosperity of workers in this country. But the research completed thus far at BLS shows some relative shift in employment toward higher-paying occupations and some relative reduction in employment in lower-paying occupations. In any case, the data show that the stereotype of jobs in the fast-growth service sector as low-paid and dead-end is not an accurate description of large numbers of the jobs in this sector.

THE FUTURE

Clearly, both the industrial and the occupational mix of employment in our country is changing. And we expect those changes to continue in the future. The most recent set of BLS projections (based on alternative scenarios of assumptions on the economy) show the service-producing sector of the economy accounting for nearly 90 percent of the projected job growth to 1995. Factory jobs are also expected to increase, but probably not to the overall level achieved in the late 1970's. Restructuring within manufacturing is expected to continue; indeed, the non-durable part of factory employment is projected to decline. And within the service-producing sector, several industries--business services, medical services, other professional services, wholesale trade, and retail trade, including eating and drinking places, are expected to account for a significant part of the job growth.

Just as employment shifts by industry are projected, important compositional changes are expected in the occupational make-up of our labor market. The most rapid rates of occupational increase are expected to take place in five broad occupational groups: executive, administrative, and managerial workers; professional workers; technicians and related support workers; sales workers; and service workers. At a more detailed level, the occupations projected to increase most rapidly are those associated with the computer, the medical service industry, and selected professional categories.

OUTPUT

The fact that the industrial and occupational composition of the Nation's work force is changing is important, but employment data, by themselves do not tell us what is happening to the Nation's output. Many people in this country have expressed concern over the possible loss of our industry output base. But employment losses in manufacturing are not always translated into losses in factory output. Real output data used in the BLS projections work show a number of interesting developments.

1. Over the last 15 years or so, when a number of the Nation's factories were losing employment, the real output of our manufacturing industry actually increased.

2. Although the BLS is projecting very small gains in manufacturing employment through 1995 (at only about one-half of one percent per year), we do expect factory real output to increase (by about three percent per year).

3. It is the share of manufacturing as a part of the total that has declined and is projected to continue to decline--both in terms of employment and output.

PRODUCTIVITY

An important factor in assessing competitive relationships is the comparative level and trend in productivity. If wages, and therefore worker incomes, are higher in the United States than abroad, we can still remain price competitive if we maintain an equal or greater productivity differential.

At the total economy level, the United States remains the most efficient country in the world, as measured by gross domestic product (GDP) per employed person. On the other hand, it is true that most other industrial countries have had faster rates of productivity growth. The gap, therefore, has narrowed. Based on the best available data, the United States now has only about a 10 to 15 percent advantage in total output per employed person relative to several European countries and about a 25 percent advantage relative to Japan.

Since 1960, real GDP per employed person has risen about 1-1/2 percent per year in the United States compared with annual rates of gain of two to four percent in Western Europe and nearly six percent in Japan. We have also experienced a productivity slowdown, from over two percent per year in the 1960 to 1973 period down to only about one-half of one percent since 1973. However, all of the other countries have also experienced productivity slowdowns since about 1973, generally equal to or even steeper than in the United States. For example, GDP per employed person in Japan slowed from about eight percent per year in the pre-1973 period to three percent per year. Nonetheless, the United States, along with Canada, still had the slowest post-1973 rate of productivity growth.

The post-1973 period includes the 1982 recession and our subsequent recovery. Since the 1982 recession, the United States has had one of the highest rates of increase in GDP per employed person--equal to Germany and only moderately below Japan. In addition, we are the only major country with a post-1982 productivity growth rate exceeding pre-1973 rates of increase. In part, of course, this reflects the fact that the United States has had a longer period of economic recovery.

If we look behind the comparative productivity growth rates at what has happened to output and employment, we see some interesting contrasts. The post-1973 slowdown in U.S.

productivity was associated with a slowdown in output growth; employment growth in the post-1973 period equaled our overall employment growth in the earlier period. Canada and Japan also had overall growth in employment, but at reduced rates compared with 1960 to 1973. The industrial European countries had slower rates of employment growth than the United States even prior to 1973, largely because of slower rates of population growth. In contrast to the United States, however, most of them experienced stagnation--or even declines--in employment in the post-1973 period, thereby counteracting, to some extent, the effect of their output slowdowns on productivity. For example, while Germany had an output slowdown of 2.7 percentage points per year, GDP per employed person slowed by only 1.8 percentage points per year because employment fell. In essence, while our productivity performance has been relatively weak prior to the past couple of years--compared to other industrial countries--we did very well in creating jobs.

GDP per employed person is a very broad productivity measure and suffers from a number of weaknesses. For example, there are no satisfactory methods of measuring the growth of real output in general government and many other service activities. Most countries, therefore, assume zero productivity growth for these sectors in measuring the growth in total output. In addition, this broad measure of productivity growth includes the effects of resource shifts among sectors with very different levels of productivity as well as the effects of individual industry productivity growth rates.

For some purposes of assessing international competitiveness, manufacturing productivity, although less comprehensive, is a better indicator. In addition, it is the manufacturing sector of our economy that has received the most attention in discussions of competitive relationships.

Unfortunately, we do not have satisfactory multi-country comparisons of manufacturing productivity levels. The available evidence indicates that the United States still has the highest average level of manufacturing productivity--although I cannot state with confidence how large this differential may be--but this is no longer true for some manufacturing industries or products.

Looking at comparative trends in manufacturing productivity--as measured by output per hour--the story is similar to that which I have described for the broader measure of real GDP per employed person. Since 1960, the United States has had a slower rise in manufacturing productivity than any of the 11 other industrial countries for which we have developed comparative measures--Canada, Japan, and nine European nations. The U.S. rate of increase between 1960 and 1984 was 2.8 percent per year, compared with about 3-1/2 percent per year in Canada, Norway, and the United Kingdom, around five to six percent in the other European countries, and eight percent in Japan.

The U.S. rate slowed from about 3-1/2 percent per year in the pre-1973 period to 1-1/2 percent per year from 1973 to 1981, then rebounded to four percent per year between 1982 and 1984. All of the other countries also experienced manufacturing productivity slowdowns that were about equal to or of greater magnitude than the U.S. slowdown. Most of them, like the United States, improved their productivity growth rates in the 1982-1984 period. Only a few, however, such as Canada and the United Kingdom, have surpassed their pre-1973 rates of gain since 1982. Nonetheless, with the exception of Canada, all of the foreign countries continued to have faster average rates of manufacturing productivity growth than the United States from 1973 forward, with Japan continuing to lead the way.

Manufacturing employment in the United States in the post-1973 period--unlike total employment--did not maintain its pre-1973 rate of increase. While the number of manufacturing jobs rose about 1-3/4 percent per year between 1982 and 1984, the level of manufacturing employment in 1984 was slightly lower than in 1973. Canada and Japan also had about the same number of manufacturing jobs in 1984 as in 1973. In contrast, all of the industrial European countries have experienced declining jobs opportunities in the manufacturing sector since 1973, ranging from nearly one percent per year in Italy to about three percent per year in the Benelux countries and the United Kingdom. In addition, for most of the European countries, manufacturing employment fell more steeply between 1982 and 1984 than from 1973 to 1981. Therefore, while European productivity growth rates continued to surpass the U.S. average rate of gain since 1973, part of their superior productivity performance was accompanied by employment and hours reductions.

While, as noted, U.S. productivity growth rates have lagged behind those of our competitors, it should be kept in mind that part of the differential reflects a catching-up process. Comparative rates of productivity growth between the United States and countries approaching the U.S. overall level of efficiency should, presumably, narrow. However, this is not a certainty, as many other factors also affect relative rates of productivity gain.

Mr. Chairman, this concludes my prepared statement. I would be pleased to answer any questions you or the members of the Committee may have.

The **Chairman**. Let me ask you just one quick question. I don't understand one sentence in your statement: "While the number of manufacturing jobs rose about one and three quarter percent per year"—this is in the United States—"between 1982 and 1984, the level of manufacturing employment in 1984 was slightly lower than in 1973."

Dr. **Norwood**. Yes.

The **Chairman**. I don't understand what that means.

Dr. **Norwood**. We've had three recessions since 1973, and so we have had up and down movements in the cycle. We have had phenomenal growth in the service industries since 1982, the end of 1982 when the last recession ended.

In some manufacturing industries, we have regained jobs. In others, particularly in nondurable manufacturing, we've continued to lose jobs.

The **Chairman**. But here is what I don't understand. Has the employment risen in the manufacturing industries roughly 1¾ percent a year, year end, year out on the average for those 12 years?

Dr. **Norwood**. No, productivity has.

The **Chairman**. It's on page 11, last paragraph.

Dr. **Norwood**. Page 11.

The **Chairman**. The middle of it:

> While the number of manufacturing jobs rose about 1¾ percent per year between 1982 and 1984, the level of manufacturing employment in 1984 was slightly lower than in 1973.

I don't understand how one follows the other.

Dr. **Norwood**. I'm sorry. Let me find that. On page 11. The last paragraph?

The **Chairman**. Yes. The second sentence in the last paragraph. I must not be reading it right.

Dr. **Norwood**. Oh, I'm sorry. Yes. That's right.

The **Chairman**. What does it mean?

Dr. **Norwood**. From 1982, from the end of the last recession, during the, in this case, 2 years of recovery, the United States has regained about 85 percent of the jobs we lost during the recession.

The **Chairman**. OK. Got it.

Dr. **Norwood**. But we have not yet regained——

The **Chairman**. We haven't quite come back to where we were.

Ms. Stern, you made a statement—instead of buying now and saving later, I think you said we have got to learn how to save now or that has to be the attitude of our companies.

Dr. **Stern**. Well, I think that there has been a great emphasis on government borrowing, with budget deficits reflecting our monetary and fiscal policy choices the last few years—starting from 1979 with our monetary policies.

But there is private borrowing there, which is also enormous, and should not be forgotten. In fact, we reached at least on a monthly basis, as I recall, one of the lowest savings rates that we have had.

The **Chairman**. That's what you meant, is this country is not saving enough. We are buying, buying, buying, but we are not saving much.

Dr. STERN. We are buying beyond our means and beyond our productive means as well.

The CHAIRMAN. Oh.

Senator Baucus has requested, as you are well aware, the ITC to do a study of the tax bill that is before us as to the effect it will have—I think probably what you are asking is on savings and how it is going to affect business capital accumulation. Do you have any top-of-the-head thoughts? I don't put you into a position on the tax bill right now, but——

Dr. STERN. No. I am delighted that we've been asked to do it.

The CHAIRMAN. Bearing in mind that the bill may be a floating target as to what it is you are studying.

Dr. STERN. Well, I think we've been asked to study Treasury II.

The CHAIRMAN. Yes, that's correct.

Dr. STERN. So we've at least got that target. And we have been in discussions as to methodologically how to handle it. I don't have, you know, a top-of-the-head statement on how it is going to affect our competitiveness. Obviously, it is going to affect different industries different ways, and I think that is what we ought to be asking.

And it may also affect those industries which are more directly in competition with imports in certain ways which may be detrimental and will not have the same kind of effect and may, in fact, help some of our service industries. And they are not directly in the line of competition with imports.

It's those kinds of questions I hope that will come out, those kind of answers and pictures which will come out of the study that we are going to do.

The CHAIRMAN. I don't know how soon we are going to have to have that. I'll know in the next few days as to whether or not the House is going to pass its bill this year, which would move our timetable up a bit next year. If the House doesn't pass its bill until next year, the whole timetable moves backward.

But you might judge the amount of time you have to work on that, depending upon what the House does in the next few days or at the outside, the next few weeks.

Dr. STERN. Very well. We will keep in touch with the committee. I think we discussed 4 months as our target.

The CHAIRMAN. Commissioner Norwood, you and I chatted just a few moments before the hearing. The stunning record of the United States in job creation—and I'm not going to argue for the moment what kind of jobs—as opposed to the common market, which has been almost static for 30 years. They just haven't gone any place.

And the Bureau of Labor Statistics did a study some time ago as to the constant dollar average wage rates in the United States, which seemed to disprove the theory that what we are doing is trading off $15 steel jobs per hour for $5 an hour McDonald Jobs. That, indeed, even with the shift of the kinds of jobs that the constant dollar per capita wage increase in the United States is an increase. It is continuing to grow up. There has been one slight dip, but it is continuing to go up. Do I paraphrase that study accurately?

Dr. **Norwood**. Well, I think the important point is that we are having both the shift in industrial composition, and a shift in occupational composition. I think most people forget that second point.

Our studies have shown that we are not having a disappearance of the middle group of workers; that, in fact, there has been some increase in the proportion in the upper-paid group. That's partly because of changes in occupational distribution as well as in industrial composition.

I think we need a lot more data than we now have in order to come up with definitive answers on that score. But I do not believe that we are becoming a Nation of hamburger makers, as many people seem to think.

The **Chairman**. Senator Long.

Senator **Long**. I want to ask you about this aspect of the problem. Some countries, Mexico, for example, choose to have a two-price system on energy; they will sell natural gas within Mexico for a pittance and they sell it outside Mexico at the market price. I think they take the attitude, well, they are flaring a lot of natural gas out there in the Gulf of Campeche, and so, if they sell it to their own company, which is PEMEX, for 1 cent per thousand cubic feet, it makes no difference that they can sell it in the United States for, say, $3 per thousand cubic feet. Their alternative is to flare it and get nothing for it, so the gas is as cheap as they want domestically. However, if we in the United States want to buy it, then it is going to cost a lot of money, even more than it would to buy it here.

If you are making ammonia, than natural gas is 85 percent of the cost, if you are making ammonia in the United States. There is no way that our people can offset the advantage Mexicans derive by selling their natural gas to themselves at zero or something in the vicinity of zero. There is no way you can compete with that.

Now I've been told by our Government, the Commerce Department, that they think that is all right. If they sell it to their own people, then they would sell it for those prices in their country. They don't feel that is a discrimination because generally it is for sale at a very cheap price in their country and there is nothing we can do about that.

We tend to have a two-price system the other way around. We will sell agricultural products high here, and cheaper on the world market. They do it the other way around.

Does it make sense to you that we should permit our industries to be liquidated when they are more efficient? We can compete effectively even with high wages until they subsidize it in a way that our Administration seems to think is perfectly all right.

Dr. **Stern**. We did a study, a section 332 study, on natural resource pricing and policies in which we described the price differentials as you are describing on petrochemicals, including natural gas. And so we do have those figures, as you are citing.

And we have also done studies. For example, we had an investigation on ammonia, and could see very clearly what was going on with the price of ammonia and other petrochemicals, as you are saying.

I recall—not from my investigative workload at the Commission but from following news accounts—that this issue got raised, I think, when we were trying to ship goods into Europe in the late 1970's that had been made with natural gas as an input—feedstock. And the argument then was it unfair for the United States which at that time was controlling the price of natural gas to use that as a feedstock for goods which were then in turn shipped to Europe.

So, in other words, the tables were turned on us. I think we've been on both sides. Now we are on the consuming side.

Whether it's fair or unfair, this is another one of those competitive conditions. Just like wages. Some of them are within our control; some of them are not. In terms of the cost of natural resources, I think that that's one of those things which, if we want to say that it is unfair—I really leave that to the policy makers like yourself.

Of course, Congressman Gibbons has that piece of legislation which has been considered. It is going to be considered again this year. I really feel that that's outside my purview as to whether it ought to be fair or unfair.

Senator LONG. You might want to comment on this. Some years ago when Herman Talmadge visited over in Japan, he made some statement at the time he left to indicate that he didn't think the United States Government was doing what it should be for our people, and someone asked him if he thought that what the Japanese were doing was wrong. His reaction was, no, he didn't think it was wrong for Japan to look after their people. He said what he felt was wrong was this nation to do nothing to look after its people while Japan was doing a very good job of looking after theirs.

Dr. STERN. I tell you, that's one reason why at least on the exchange rate issue, which is another kind of competitive advantage which we ourselves have given the rest of the world with our dollar, is something we can do something about here at once. And that's one reason why I have tried to drive this issue home. That's not to say that there may be other areas in which other countries find themselves more competitive vis-a-vis the United States when it comes to selling——

Senator LONG. When I think about the exchange rate, I find myself thinking, well now, just that one item—and I'm not sure that that's all there is to it—but just that one item is a very big competitive advantage that this Nation gave to foreign importers for a political reason. And if the United States wants to do that, it ought to give some consideration to the people who are being crushed and destroyed in this country by that policy.

Sometimes we do things of the nature: We will pass a law that has to do with taxes, and someone will say, well, wait a minute, that could put us out of business because it runs up our cost on the foreign market. So we can say, as we tend to do sometimes, all right then, we will give you the money back at the border if you are exporting so it won't hurt your competitive position.

If we are going to engage as a political decision in that type of monetary policy or fiscal policy, because it's a mix of the two, we ought to take a look at all of these people who are going to be suffering from that, and take appropriate action to see that if we cannot justify victimizing a group, that group is not hurt by our action.

Dr. **Stern**. I'm seeing those industrial and agricultural casualties of those decisions. That's basically the reason why I go back to the root cause of it.

Senator **Long**. Thank you.

The **Chairman**. Senator Baucus.

Senator **Baucus**. Dr. Stern, as I understand it, you are basically saying that apart from the problems of the dollar and exchange rates that as important as it is to address unfair trade practices that other countries may engage in—that is very important—the more important underlying reason is the lack of U.S. competitive position and underlying U.S. competitiveness. What do you mean by that? I mean could you identify some areas where you think the United States has not sufficiently addressed its underlying competitive position? Give us some examples so we can flush that out a little bit.

And maybe in answering, you could tell us what you mean by competitiveness. I mean what's your definition of competitiveness?

Dr. **Stern**. My definition of competitiveness uses an international standard. Can we compete? Say we had this flat field that everyone is looking for, can we compete out there?

The dollar, as you said, is something which I have emphasized in the past. It is something which even though we may be doing something about it now is still going to leave us in difficult shape to compete. Even before the dollar strengthened, we've had many troubled industries. For example, the auto industry; you are going to hear from Mr. Bieber after us.

The auto industry came to the Commission complaining about import competition in 1980 before anyone was ever complaining about the dollar.

Senator **Baucus**. What specific examples do you have?

Dr. **Stern**. I think that we have to talk about wages. I think we have to talk about investment decisions; whether we are going to go for short-term profits and short-term bonuses in some of these industries or whether we are going to plow profits back into the industry to invest in labor-saving devices, robotics. In many cases, that is going to result in increased capacity. In going for robotics it's also going to mean that workers are going to be bearing a great brunt in the adjustment area, and that we have to then devise an adjustment policy that makes sense for those workers who are necessarily going to be affected by decisions such as that.

It also means going for volume instead of just going for price. It means looking at the ways in which we can focus not just on the imports as the problem, but some of the home-grown generated costs. And we have to become much more willing to market worldwide instead of market just to the United States. This is a job for business itself. Business people have got to realize that while we have had this very comfortable domestic market here for many years, it's no longer the case. We have enormous increasing import penetrations, and we to have to now go overseas for our markets.

Senator **Baucus**. And I agree with you.

Dr. **Stern**. Moreover, quality has to be increased. There has to be less tolerance for shoddy production.

Senator **Baucus**. Commissioner Norwood, you addressed a point which I think is on the minds of most people probably in this room, in this country. That is, are there too many new service jobs compared with basic underlying manufacturing jobs. The trend is in the wrong direction for the long-term health of our country.

You mentioned that not all service jobs are bad jobs. You seemed to imply that a certain number of service jobs, new service jobs, are bad jobs. And I have two questions to ask you.

First, what percent of the new jobs are not bad jobs? And you could identify where those are.

Second, how do you define bad anyway? Because even though you think that certain jobs are not bad jobs, isn't there a good argument that the more we move into a service economy and the more we move away from a manufacturing-based economy that we are in the long term robbing future viability and health of this country because of manufacturing jobs are going overseas and we are keeping only service jobs in this country; that we are destroying the technological development, advances in new technologies, and we are also putting our country in great peril, in great jeopardy, national security base and all kinds of reasons that we should not—that we should be alarmed about the increase in service jobs anyway.

Dr. NORWOOD. Well, I disagree with that.

Senator BAUCUS. And why do you disagree?

Dr. NORWOOD. Well, let me first answer your specific two questions.

Senator BAUCUS. Sure.

Dr. NORWOOD. What is a bad job? I personally would define a bad job as those which are part time; not full-time jobs, don't have much of a future; they are dead end, and they pay very little.

Where are they? We all know that we have a lot of them in one of the fastest growing industries in this country; namely, eating and drinking places. If you look at an input-output table which gives you relationships of job requirements per so many dollars of output, and you look at some of the defense output increases in terms of dollar expenditures, you find that one of the things that does tend to increase is eating and drinking places. And that happens with any expansion in the country.

I think the important point is not how many jobs we have in manufacturing. The important point is how effective we are at developing outputs from our manufacturing industries.

If we can produce with fewer workers by being more efficient and if, at the same, we can have jobs for those workers in other industries, then it seems to me that the country as a whole is not worse off. It is true, as Commissioner Stern pointed out, that we have got to have programs to permit some flexibility, some adjustments for those workers. But the fact that a worker may lose a job in one industry, if there is another job that is a good job for him, and if we are at the same time keeping up our manufacturing outputs, then it seems to me that that's not a problem.

There are a few industries where we are not doing that. Three decades ago we began losing jobs in apparel and textiles, in shoes, in leather.

Those are not industries which are keeping up either employment or output. But you will find in many of our other manufacturing industries that we have lost employment, but we have not lost output.

Senator BAUCUS. So you basically think that there is a problem if we are losing output in those basic manufacturing industries. It seems to me if we are losing output, we are probably also losing jobs. It's right to focus on the output.

And I see my time is up. We can get back to this.

The CHAIRMAN. Senator Bentsen.

Senator BENTSEN. First, Mr. Chairman, let me thank you on the quality of the witnesses. You've got a couple of good ones.

Let me say, Dr. Stern, now that I have said that, let me drop the other shoe. You have emphasized that unfair trade is not really the problem of the trade deficit. I don't think it's the biggest problem, but I think it's a very serious problem.

You have also said that about a 5 percent of the total value of U.S. imports has been challenged before the Commission. And that comes out to the figure of around $17 billion.

Now the recent national trade estimate contained 250 pages of unfair foreign trade barriers. The best estimate I have been able to get on that one as far as the value is some $25 to $30 billion. That adds up to about $45 billion.

Now when you have got those kinds of unfair barriers and you have subsidized goods coming into this country, don't you think it's worth a national effort to try to bring about a correction in those, if we can?

Dr. STERN. Absolutely.

Senator BENTSEN. Now the other question you talked about is improving competitiveness, you think the United States should tie modernization to utilization of the escape clause. And I sure agree with that. But how do you approach the situation where you do that and then you have individual companies that don't comply? How would you suggest we apply ourselves to that in a legislative way?

I'm with you on your objective. It's just how do you administer that?

Dr. STERN. Well, I'm still grappling with this as well. And thinking out loud, I think of what I understand to be Japan's recession cartels or depressed industry cartels. As I understand it—and I'm not saying we should do what Japan does, but I think it's worth taking a look at it to see if there are any kind of clues. That he who benefits should also participate. And if you do not want to participate in the revitalization plan, then you will not benefit from their antitrust administration.

Now what they do, as I understand it—and I stand to be corrected—they don't administer the antitrust laws as we do; they get these firms together; they say capacity in the industry will be this; your individual capacity will be this; the prices will be raised during the period of this protection; imports will be restricted—I beg your pardon?

Senator BENTSEN. That's pretty difficult for us to do under our system.

Dr. STERN. Well, I think that there has been some discussion about looking at antitrust exemptions during a certain period of relief. But I think that while we may be looking on the ledger of increasing ways in which the Government can help out troubled industries, I think we also should expend some energy on making sure that those industries, if they are going to get increased benefits in addition to import relief, antitrust exemptions, or even stretch ours in compliance of environmental regulations, tax policies that may get a special looking at, that the businesses and the workers, too, ought to have to come to the table and say what they are going to be doing. And that gets to what they are going to be doing with the possible initial increased price effects of the kind of revitalization plan that would be envisioned.

Senator **Bentsen**. Well, I appreciate that, and I think that's a contribution.

Now, Dr. Norwood, you were talking about service jobs. And I've heard a lot of talk about the creation of 8 or 9 million service jobs in this administration, which is fine. I think that's good.

But I also remember that there were millions of service jobs created in the previous administration, too, and I think that was great, too. And I think those jobs are very necessary, and I think there are good ones and I think there are bad ones.

But what concerns me is the fact when you are talking about services, the producer normally has to be close to the consumer. And I don't see the creation of wealth by increased jobs in the service industry, to the extent I see it in manufacturing. And I look at the Bank of England's report—I saw it in the Financial Times, the last quarter of the Bank of England report—where it talks about the fact that manufacturing jobs are absolutely indispensable. Yet you have seen this growth in the service sector. A lot of it in travel.

And the question: Does that really increase the standard of living? Does that really increase wealth? And if you have got a service that's exportable, then you provide the service abroad and you may get something back from the franchise, but the jobs are often created over in the other country.

So only a small proportion of the output of services is really traded internationally. And that's my concern with the move toward job creation in the service industry.

Dr. **Norwood**. Well, I think we do have jobs, as you quite rightly point out, in the service sector. Many of them are in internationally traded industries. But you are right in worrying a bit about this distribution of many of these industries. Services have tended to grow up around goods-producing areas where there are a few plants, and there are feeder plants, and then there are the services that go with that in a particular area of the country.

And I do think that we are going to be seeing much greater disparity from one local area to another within this country, although we may on average seem to be doing——

Senator **Bentsen**. The point I'm really getting to, though, is I don't see services exported to the extent of manufactured goods insofar as transferring wealth back into this country. Some of it, of course, but I don't see as big a correlation there.

Dr. **Norwood**. Senator Bentsen, let me say that I am not certain that—I guess I had better be a little careful in how I state this.

Senator **Bentsen**. You usually are.

Dr. **Norwood**. I'm not certain that the data that we classify as services is all services. Let me just tell you that yesterday I was in Parkersburg, WV, visiting one of the very large chemical plants there. And I asked about contracting out. And I found that a number of activities which formerly had been done by the company itself were now done by contractors for a variety of very good reasons.

We, nevertheless, are putting those jobs, many of those jobs, in the standard industrial classification that involves services.

Senator **Bentsen**. Well, it's the same report.

Dr. **Norwood**. That's a matter of some real concern to me.

Senator **Bentsen**. This same report says that the adequacy of information on what really are services and being exported is really very limited.

Dr. **Norwood**. That's right.

Senator **Bentsen**. And not too reliable. And that's the point you are making.

The **Chairman**. I just want to make sure I understand something. They contract out the jobs. They used to be called manufacturing, and they are now called services although it's the same job.

Dr. **Norwood**. Well, that's right. In some cases there were legal services, accounting—payroll, for example.

The **Chairman**. But if they all were employed by the chemical company, you would count them all as manufacturing jobs.

Dr. **Norwood**. Right.

The **Chairman**. I see.

Senator Mitchell.

Senator **Mitchell**. Thank you, Mr. Chairman.

Dr. Stern, you are familiar with the circumstances of the footwear decision in which the Commission decided unanimously that the domestic industry is being injured by imports and recommended by a 4 to 1 vote relief which the President rejected. What effect do you expect the President's decision to have on section 201 cases? Why should any industry now follow the section 201 route? Why should anyone go to your commission when an industry that now suffers import penetration of 78 percent has been denied relief?

Dr. **Stern**. Well, we've had two cases filed since the President's decision, so there must be some people who feel that it is a fruitful route. I can't second-guess them. I haven't even looked at the merits of their cases on the question of is there serious injury and are imports the most important cause or at least as important as any other cause of a serious injury or threat.

I don't need to tell you, but the President, of course, looks at a much broader range of considerations when deciding whether to take a Commission recommendation. We just look at the industry and the impact of imports on that industry. He has to look at national economic considerations, considerations of consumers' cost, diplomatic considerations, other considerations.

I suspect that there must be some industries who feel that they can convince the President once it gets to that Presidential level more successfully than the footwear industry.

As I look back on the figures, at least this President has taken Commission relief more times than he hasn't or taken a recommendation to give import relief more times than not. And, of course, there was one time in the case of the auto industry where the Commission majority found that imports were not the most important cause of a threat of serious injury and relief was given.

Senator MITCHELL. Indicating that——

Dr. STERN. The figures of the ITC.

Senator MITCHELL. The category which you describe as other considerations frequently dominate.

Dr. STERN. Well, you are closer to that than I am.

Senator MITCHELL. You are very courteous to describe them as other considerations. Some others, including myself, would describe them as political considerations, domestic political considerations.

Dr. STERN. And, of course, I've written a book on the subject of how domestic politics influence our foreign trade policy so I have great respect for that consideration as well.

But it is not within the purview of the ITC.

Senator MITCHELL. Well, I think you will find increasingly that American industries will not use that route for the obvious reason that the Commission's recommendations have very little relevance in this administration. I think that's an unfortunate fact and will ultimately diminish the role of the Commission.

I'd like to ask a question about a specific reference in your testimony. On page 5, you make reference to countervailing duty and antidumping cases, and state that dumping and subsidization of imports are unfair only if shown to materially injure a U.S. industry. You are familiar with that portion of your testimony. It's the end of the first paragraph on page 5.

What about a case where a foreign government's practices interfere with U.S. trade in third-country markets? And you are responsible for determining the effect of imports on domestic industries, are you not?

Dr. STERN. In U.S. markets.

Senator MITCHELL. In U.S. markets only?

Dr. STERN. Yes, sir.

Senator MITCHELL. So you can't look at that at all?

Dr. STERN. That's correct.

Senator MITCHELL. In your judgment, should our trade laws be revised to permit that factor to be taken into account? Can you fairly judge the effect of a practice on U.S. industry if it is limited only to the effect within U.S. markets when, in fact, the practice may have a materially injurious effect on U.S. industry that is competing in a third-country market?

Dr. STERN. We are not supposed to weigh causes in a dumping or countervailing duty case. If there has just been material injury by reason of these unfair trade practices, that is enough for an affirmative.

But there are times when I will see an industry which is feeling that it has been injured by these unfair practices in the U.S. market by dumping or a subsidization but it has been exporting as well, and it has lost market share overseas.

We will try—I will try to ask them to give some figures on how much of their profits have been eroded by loss of market share overseas just to kind of get some idea. Again, I'm careful not to weigh that as a possible cause of the injury against the dumping or the subsidization, but I am interested in how that might be making the industry vulnerable to dumping in the U.S. marketplace.

I think that the Department of Commerce, of course, has been equipped to go overseas. We have not. We do not send our people overseas except on special missions that the Finance Committee asks us to do on special studies, such as the natural resource pricing and policies of other countries.

It is something which, I suppose, is doable, but we are not equipped to do it on a regular basis.

Senator **Mitchell**. Well, my time is up.

Could I just ask, Mr. Chairman, if Dr. Stern would provide to the committee a written summary of the decisions regarding 201 made since January 1981 and the outcome of those? You've made a general statement that the President has accepted more than he has rejected.

Dr. **Stern**. Be happy to.

Senator **Mitchell**. And it would be helpful, I think, to have that in summary fashion.

Dr. **Stern**. Absolutely. We've got that.

Senator **Mitchell**. Thank you, Mr. Chairman.

[The information from Dr. Stern follows:]

SECTION 201 CASES SINCE 1981

Case	ITC decision	President's action
1981		
Fishing rods.	No injury.	
1982		
Tubeless tire valves.	No injury.	
1983		
Motorcycles.	Tariff increase.	Tariff increase.
Stainless steel.	Quotas.	Quotas and tariff increase.
1984		
Flatware.	No injury.	
Footwear.	No injury.	
Carbon steel.	Quotas/tariff increase.	OMAs negotiated.
Copper.	Tariff inacrease or quota.	No relief.
Tuna.	No injury.	
1985		
Potassium permanganate.	No injury.	
Footwear	Quotas.	No relief.
Shakes and shingles	Pending.	
Electric shavers	Pending.	
Cast metal products.	Pending.	

The **Chairman**. Senator Danforth.

Senator **Danforth**. One of the subjects of increasing attention is going to be the extent of discretion that the President should have in section 201 cases. Now let's take a couple of hypotheticals. Let's take an industry which is by nobody's imagination an essential industry. Let's say that it makes hoola-hoops and that it is clearly being injured by imports. No doubt about it. Ninety percent import penetration for hoola-hoops. And let's suppose that all hoola-hoops are made, say, in Egypt, and that it's an important ally of the United States, and if the hoola-hoop trade is in any way affected, Egypt is going to go down the drain.

Now that is one type of hypothetical. Another type of hypothetical would be a basic U.S. industry. Let's say shoes. [Laughter.]

And let's say shoes are absolutely essential and that, you know, everybody knows that an army doesn't march on its stomach; it marches on its feet. And that we have to have shoes. And the shoes are made all over the world and there is no place where it is the essence of the economy of another country.

I guess the question is: How should that kind of difference between types of products, their essential nature, the effect of their trade on other countries, factor into our decision making on import relief without getting into the kind of situation that we are in now where there is so much discretion in the hands of the President that a president—not pointing to any particular one, but a president could deny import relief on purely philosophical grounds? The president could say, well, "I'm a free trader; I'm against Smoot-Hawley, and section 201 is the Smoot-Hawley provision, and, therefore, I'm not going to use Section 201; I don't care what the ITC does, I'm not going to do it."

How and where can a decision be made that in some cases we should grant 201 relief, import relief, on policy grounds without creating so much discretion that a very ideological president could simply say, well, "We don't care about what Congress does, we don't care about what the ITC does, we are not going to utilize the statute?"

Mr. **Stern**. That question is for Commissioner Norwood, isn't it?

Senator **Danforth**. For both of you, really. I'd just like to find out any thoughts that you have—leading to possibly a change in the law so that we don't have a deadend street, as per Senator Mitchell. And I happen to concur with him. We believe that section 201 is a deadend street.

Now I don't want to get into that discussion. But let's suppose it is. Or let's suppose that in the future it could be just by a president saying I'm never going to use it.

Dr. **Norwood**. Senator, I'm going to leave that question for Commissioner Stern since I stay out of policy issues. But some years ago I did do some work in the trade field, and I did some careful review of the old Tariff Commission decision.

And one of the things that struck me was the fact that escape clause cases of various kinds of escapes were being looked at with no consideration really of the size of the group of people who were affected. And it seems to me that to consider a decline in an industry which is small compared to an industry which is extremely large, which we certainly used to do—perhaps under Chairman Stern's direction the Commission no longer does that—I think that that is an important consideration we need to look at.

Dr. **Stern**. Getting to your question, you have touched on three points. One is the president's discretion and how much to allow him. One is the question of national security. One is the question of the purview of the ITC.

I'll leave the national security consideration aside for a minute.

Senator **Danforth**. I'm not really talking so much about national security, but by anybody's definition would be an essential industry.

Dr. **Stern**. I think what happens now is that the way the Commission mandate is we can basically recommend quotas. Adjustment assistance is fraudulent to recommend because there is nothing there. And tariffs have been swamped by the increasing dollar over the last 5 years, so that relief is not effective. So we are left with quotas.

And when the president gets a recommendation from the Commission, it's quotas and it's like take it or leave it, at least if ideologically you are not interested in looking at the competitiveness of the entire industry.

I think we should be permitted to recommend much more comprehensive recommendations to the president not just on the import side, but on all the other things that impact on the competitiveness of the industry. And then you might have the President comment if he's going to act or not act, and if he's not going to act, why isn't he going to act, on every one of the recommendations that we make.

Even sometimes when imports may not be the most important cause of serious injury or threat of serious injury, because there have been cases, for example, in the carbon steel industry where I have found that there were other causes which were more important than imports. That's not to say that imports weren't important. And that's not to say that you should walk away from the important issues.

But the way it is constructed now, if the president wishes, he can walk away from the industry—even when imports are an important cause of serious injury, and even parenthetically when the industry is a large industry.

Now the law on large and small is very clear. It's also very clear on cyclical or noncyclical. We are not supposed to make it easier for a larger industry than a small industry to get relief. We are not supposed to make it easier for noncyclical rather than a cyclical industry to get relief. We are not supposed to be doing that. That is not within the ITC's purview, but if it's the president, again, for political, and I say political with a big "P" should take into consideration whether it's big or large or what the employment impact is going to be as well as the consumer impact. Whether it's an end user—if steel users are going to be using protected steel.

That has not been the ITC's job. Now that's not to say that we can't if we are asked to comment on it, but the Commission has been very cautious in going beyond what is a narrow mandate in the law. And that law has reflected the fact that escape clause actions were really not that important up until now. Trade wasn't that important up until now. But now is the time to look and see whether we ought to re-equip ourselves.

I think that we could do a lot better than just giving the President a take it or leave it option. Make it more palatable.

Senator **Danforth**. Senator Bradley.

Senator **Bradley**. Thank you very much, Mr. Chairman.

I would like to explore with you a little bit the possibility of building some structural adjustment into our policies that seek access to foreign markets. Right now we have a section 301 procedure that determines if there are unfair foreign trade barriers, and then the U.S.T.R. is instructed to negotiate to try to resolve any dispute if, indeed, there is an unfair foreign trade barrier.

We have a section 201 procedure that deals with whether imports coming into the country injure an industry.

One of the things that I've been thinking about is whether there is any way that we can link those two procedures. For example, is there any way that we could give expedited action to an exporter seeking to knock down a foreign trade barrier if that exporter would be willing to help an import-sensitive industry adjust?

Dr. STERN. I have read your legislation, and I think that I can see it making more sense politically. I think it's going to be hard to get industries together to marry, if you will, their interests. The import industry which is very large won't be interested in dealing with an export industry which probably has a losing case overseas. It's going to be very hard to even force that kind of a marriage.

But I guess I go back to the fact that we have just got shrinking trade worldwide. And it seems to me that if you are going to kind of pick up these kind of opportunities, we are going to have to go back to some of the root causes of why we have world trade which has practically stagnated since 1980.

Senator BRADLEY. But my point is that if you believe in a rules-based multilateral trading system and you have national laws that seek to implement that kind of trading system, and those national laws don't function for one reason or another, then they need reform. Rather than real reform, we have examples of the ITC finding injury and the president deciding not to provide relief.

If you don't make the multilateral system work, then you are going to have to accept barriers that act as a tax on that system. Whether you find an export industry that could find an import-sensitive industry or not is a question that will only be resolved from the experience of having the law go into effect.

I don't see any down side in doing this. Do you?

Dr. STERN. I don't see any down side. No, I don't.

Senator BRADLEY. It seems to me that that is an extremely important point. If now you can't get access to markets, you need some kind of sanction, such as import relief for industries sensitive to imports from the country to whose markets you are seeking better access.

Dr. STERN. Well, I can see that that is obviously something which is taken into account at least by our foreign trade partners when we do want to restrict access. I mean they have to decide in what way they are going to retaliate, and what way they are going to make it easier on us to not put the relief into place.

Senator BRADLEY. You know, if I were Japan and I had barriers to pharmaceutical imports from the United States and I were faced with barriers to my exports of whatever to the United States until I removed my barriers against pharmaceuticals, I might be more inclined to settle.

Dr. STERN. That's right. I suspect that is happening now, but I guess what you are saying is you would like to kind of push it as a way of reinforcing our negotiators when it comes time to telling these countries that——

Senator **Bradley**. And also recognizing that the exporters would be willing to help that import-sensitive adjust after any period of temporary import relief.

Senator **Danforth**. Any further questions of this panel?

Senator Baucus.

Senator **Baucus**. I wonder if you could explore a little bit more the question that Senator Danforth asked. That is, how to change 201 because I think there is a perception in this country that it is just not working for various reasons. The president, because he has so much discretion, decides on a basis which sometimes doesn't have that much to do with the proceeding before the Commission.

What would your reaction be if Congress passed legislation saying that where industry and labor agree upon solutions or recommendations of the ITC that the president is required to grant relief which is substantially equivalent to the recommendations by the ITC, assuming they gave a recommendation and assuming further that industry and labor agree that that's a proper solution? Would it make sense in that case to limit the President's discretion? In the way I have outlined; that is, where he has to grant substantially equivalent relief.

Dr. **Stern**. I believe—again, I should make it very clear that I am speaking for myself; not for the Commission on any of these responses to your questions—that there are good reasons why the President of the United States who is elected by the entire Nation should have discretion to exercise the vast Presidential powers that are available to him, discretion beyond that of appointed officials at the International Trade Commission.

I am a little wary. I believe that there are ways that we can make section 201 a better piece of equipment so that we can make a more comprehensive recommendation to the President; that you could discipline the decisionmaking, the discretion at the Presidential level so that you would have greater satisfaction that there is a competitive look at the industry.

But I feel very uncomfortable taking the discretion away from the President. I have seen, for example, ways in which the Tariff Commission, which used to make the adjustment assistance determinations years ago lose that job. People were not happy with the way the decisions were being made at the Tariff Commission. Then criteria were changed, but it was also given to the Department of Labor. The same thing happened when people were not happy with the Department of the Treasury in decisions on dumping and CVD cases.

Senator **Baucus**. What would your action be if the legislation were to require the ITC to look at all the causes that caused injury? That is, to look at and identify the degree to which industry's ability to sell overseas is also a cause.

I mean should the ITC's jurisdiction be broadened to look at other causes?

Dr. **Stern**. Yes. Oh, we are supposed to in section 201 weigh other causes to see whether imports are as important or at least as important as any other cause of serious injury. So we should be. But the problem is we seem to stop because once we have found that imports are as important as any other cause of injury or threat, then we just focus on that import relief as the answer. And, as I said, the menu has been limited now to just quotas because the other things have been removed effectively.

So I think we should be commenting and recommending what ought to be done about the other causes of competitive problems in the industry. Some of them have to do with cost structures within the industry. Some of them had to do with our own macroeconomic policy, and I mean the cost of money.

Senator **Baucus**. And you would also suggest that the President be in legislation required to delineate his responses to certain points made by the Commission.

Dr. **Stern**. Absolutely. I think that that would be very important in kind of disciplining the process.

Senator **Baucus**. In the remaining time, could you elaborate briefly on your point about auction quotas; using that as a potential way to——

Dr. **Stern**. Well, as you know, the Commission recommended it in the footwear case, and the idea died when the President decided not to give import relief in that case.

It is an effort to recapture what you might call the rents from the quota that have gone offshore to our foreign competition. When the amount of goods in the country are limited, the costs rise. There is a price effect which is captured both by the industry that is protected here—in the auto industry, we figure that the revenues that were captured by the U.S. auto producers were about $9 billion from the price effect. But, meanwhile, the Japanese producers overseas got more than half—got about $5 billion worth of benefits from that voluntary restraint agreement. That went to retooling the Japanese competition to compete once the import relief was removed.

By auctioning off the qutoas which are given free of charge now, you could recapture that into the revenues of the U.S. Treasury and plow that back into either helping the workers who are the ones we have been talking all morning about—the fact is that the workers are bearing the brunt of all this adjustment that we are talking about here. They are bearing the immediate brunt. And they are getting the greatest shaft right now, I think. And that kind of recapturing of those quota rents could then be plowed back into helping those workers retrain, remobilize, and in certain cases retire earlier, but more comfortably.

We have used figures that you are going to hear from Gary Hufbauer later today. He has figures that show that if you auctioned off the 10 top areas that are now being protected with quotas free of charge, you would get $6 billion recaptured for 1986 alone. That's significant.

Senator **Baucus**. I think it's a very useful idea that we will have to explore more fully. I see my time is up. Thank you very much.

Dr. **Stern**. Thank you.

Senator **Danforth**. Senator Chafee.

Senator **Chafee**. Miss Stern, on the auction business—and I regret that I wasn't here earlier. I was testifying before the House on another matter. But the auction proposal, as I understand it, would work as follows: If we are going to increase the automobile import quotas that were previously levied only against—well, they are levied against any imports, but the only people really hit by them were Japan because they were the country that qualified under the terms of the quotas. But what you would do is auction these off to Yugoslavia and Korea and Japan and whoever wanted to bid?

Dr. **Stern**. Whoever wants to bid. And the ones who are most competitive in the world marketplace, theoretically, would be able to bid highest, and you would also, therefore, attract the most competitive products in first rather than say having those who have historically been in the marketplace keep their historical spot in the marketplace.

Senator **Chafee**. Well, now who would do the bidding? Would the government of Yugoslavia do the bidding?

Dr. **Stern**. That's what is happening now when you tell a country that they can't ship in any more than *x* amount of widgets. In effect, the Government of Transylvania is telling its producers you can bring in this much, you can ship out that much. We would have to have someone administering this, the Department of the Treasury or someone else. That's the whole point of capturing the revenues here.

Senator **Chafee**. Restrict it to the automobile situation because that was a particular situation that we had. We had quotas.

All right. Now how would that work in that particular case?

Dr. **Stern**. OK. Say you want to ship in goods. How much will you pay for it? It's like getting a license to import. That's what a tariff is. You would get the kind of price effect that you would get from a tariff, but you would have the bidders saying how much they would bid in order to have the license to come into the United States.

Senator **Chafee**. The companies or the countries?

Dr. **Stern**. I think whoever has the goods. If the companies give their government the authority to bid for them, I suppose you could have the government authority.

Senator **Chafee**. So South Korea would submit a bid, Yugoslavia, on automobiles, for example.

Dr. **Stern**. If Yugoslavia is producing autos.

Senator **Chafee**. Yes, they are producing.

Dr. **Stern**. I mean you would have to be able to deliver the goods. I mean if you are going to pay for it, obviously, you would have the goods.

My belief is that the business people ought to make a deal with the marketplace. But if they can't make a deal with the marketplace because of political reasons, economic reasons, reasons that are defined in the law, then they have to make a deal with the government. If they are going to make a deal with the government, I think we should at least be very frugal in making sure that the kind of deal really helps the United States, and helps the firms that are getting this kind of protection.

We have not done a study on how to administer it.

Senator **Chafee**. Well, I don't want to beat this to death, but it's a suggestion you have come up with and, obviously, it's worth considering.

It seems to me that the Japanese would be the big bidders. They are the people who are in the game, and they would bid for the quotas we are auctioning off. But your answer to that is, well, fine, but we get some revenue from it.

Dr. **Stern**. We recapture the revenue, exactly.

Senator **Chafee**. We being the U.S. Government.

Dr. **Stern**. U.S. Government, exactly.

Senator **Chafee**. Now what does that do for the Chrysler worker who is thrown out of a job because the import quotas go up?

Dr. **Stern**. No difference. The protection would be no different than what it was, the way it was administered in the last 4 years from 1980 to 1984. That's up to the creativity of the policymakers, and that's the other questions that I've been answering here today. The creativity of the U.S. Government when it comes to dealing with those workers who are bearing the greatest brunt. And that's where we have to be——

Senator **Chafee**. Would that be GATT-compatible in your judgment?

Dr. **Stern**. Beg your pardon?

Senator **Chafee**. Would that be compatible with GATT?

Dr. **Stern**. Our general counsel did a memorandum for the Commission before we were willing to make this recommendation to the President and we were satisfied as a Commission that it was permissible.

Senator **Chafee**. Thank you.

Thank you, Mr. Chairman.

Senator **Danforth**. Thank you both very much for excellent testimony.

Senator **Mitchell**. Mr. Chairman.

Senator **Danforth**. More questions?

Senator **Mitchell**. If that is permissible.

Senator **Danforth**. Thank you for what will be good testimony. Senator Mitchell.

Senator **Mitchell**. Dr. Stern, as you know, section 301 is the trade remedy statute that authorizes the president to take appropriate action, including retaliation, to obtain the removal of:

> Any act, policy or practice of a foreign government which violates an international trade agreement or is found to be unjustifiable, unreasonable, or discriminatory and which burdens U.S. commerce.

Do you know how many times since that law was enacted a decade ago, that actions have been brought under it?

Dr. **Stern**. No, sir. It's not within my purview.

Senator **Mitchell**. Right.

Dr. **Stern**. But it's my feeling that there have been 301 cases occasionally initiated, the specialty steel case was certainly one. And there have been some agricultural cases, I think, on almonds and raisins.

We can get that, if you would like.

Senator **Mitchell**. Would you get that?

Dr. **Stern**. Gladly.

Senator **Mitchell**. And also the number of occasions in which it has actually been invoked.

Dr. STERN. Well, that, I think, was rarely invoked, but it has been accelerating the last couple of——

Senator MITCHELL. Does once in 11 years sound right to you?

Dr. STERN. It sounds about right, yes. It certainly has accelerated in the last couple of months.

Senator MITCHELL. And if a trade law has been on the books for 10 years and invoked only once, would it be a fair conclusion that the law is not accomplishing its purpose and should be changed to accomplish its purpose?

Dr. STERN. Yes; I think it's also important, though, when you try to change the law to accomplish the purpose that you get right to how to do it. That's why I was going back to this business about changing the agency that does the job.

People weren't happy with the Treasury Department. Congress set deadlines in dumping and CVD cases, but then gave the job to the Commerce Department. Probably, they would have been happy eventually with Treasury if they had just had those deadlines put on them.

Senator MITCHELL. Well, what suggestions do you have for making this law work?

Dr. STERN. Again, it has not been within our jurisdiction and so I have not put on my thinking cap to the extent that I have on section 201. It was considered to give it to the ITC back in 1980. There was a serious consideration, and so we rushed around for about a week or two to look into it. But we really have not done that kind of work.

Senator MITCHELL. Well, I'll be joining other Senators under Senator Danforth's leadership today to introduce new trade legislation. And one of the titles which I will be introducing would expand the list of actionable practices under section 301 to permit retaliation against targeting practices such as export subsidies to third markets, import restrictions, export performance requirements, trade restraining agreements that divert trade to the U.S. market if an industry protection or the denial of fair and equitable relief can't stand our competitive practices.

And what I would like to ask you to do is, if you would—you are an expert in this area, although you don't have jurisdiction over this law—take a look at the proposal and give the committee your written views on whether or not you feel these changes will improve the law.

My feeling is that if trade laws don't work, if they are not utilized, then it's worse than having no law at all because they create the illusion of a remedy where none exists. If someone sits down and reads section 301, they would think that there is a remedy available in this country against unfair trade practices by foreign governments. But, in fact, if the law is never invoked or enforced, then, of course, there is no such remedy. And I think we ought to either make these laws work or do away with them.

[The information from Dr. Stern follows:]

WANG No. 1787C

301 Summary

There have been 51 petitions accepted and investigations instituted pursuant to section 301 of the Trade Act of 1974 (19 U.S.C. § 2411 et seq.) between 1974 and November 1985. Each of these investigations can be considered action taken by the President under section 301. In a large majority of investigations there has been consultation with the other country under provisions of the GATT or one of the other Non-Tariff Measure Codes (e.g., Antidumping Code, Subsidies Code, Standards Code, etc.) and some sort of resolution has been reached and the investigation terminated.

Section 301 provides authority for the President to retaliate against other countries or instrumentalities that discriminate against U.S. commerce. In only two instances involving three investigations have there actually been retaliatory measures instituted. In investigation number 301-15, Certain U.S. Television Licenses, a petition was filed in August 1978 alleging that certain provisions of the Canadian Income Tax Act were unreasonable in denying tax deductions to any Canadian taxpayer for advertising time purchased from a U.S. broadcaster for advertising aimed at the Canadian market, even though the Act permitted deductions for advertising time purchased from a Canadian broadcaster. Since this was an investigation involving services, there were no relevant international agreements providing for dispute settlement procedures. Public hearings were held and on August 1, 1980, the President determined that the most appropriate response was U.S. legislation that would mirror the Canadian law. The U.S. legislation was enacted on October 30, 1984.

The second instance of retaliation involved investigation number 301-11, begun pursuant to a petition filed by the Florida Citrus Commission and others in November 1976 alleging that the European Community discriminated against imports of U.S. citrus products. The dispute was taken to the GATT in 1980. A full GATT panel report was submitted in December 1984 supporting the U.S. position, but the EC blocked any action. On April 30, 1985, the United States stated that it considered the dispute settlement process completed. In retaliation the President announced a substantially increased U.S. duty on imports of pasta from the EC, effective November 1, 1985. In effect, this retaliation also applies to investigation 310-25, which was begun pursuant to a petition filed in October 1981 by the National Pasta Association concerning EC export subsidies on pasta exports. It is worth noting that the EC instituted a counter-retaliation in the form of increased duties on imports of American lemons and walnuts.

The United States has also acted to subsidize sales of American wheat flour to Egypt in response to EC subsidies. Though there is a long-standing section 301 investigation on this issue, investigation number 301-6 (petition filed by the Miller's National Federation in November 1975), the American sales were made under the authority of the section 5(f) of the Commodity Credit Corporation Charter Act (19 U.S.C. § 714c(f)), and were not characterized as retaliation pursuant to section 301.

AMENDMENTS TO SECTION 301

It is not easy to generalize from my experience in dealing with unfairly traded imports to dealing with unfair practices that hurt U.S. exports. In the former case, we do not have to seek removal of the unfair practice, as the domestic industry's injury can be remedied by the imposition of a duty, through the antidumping or countervailing duty laws, that offsets the effect of the unfair practice. With regard to exports, however, the most satisfactory solution will usually be the termination of the practice by the foreign government. Obviously, this is a much more difficult task.

Regarding your bill, I understand that it would include a number of specific causes of action in section 301 of the Trade Act of 1974. These include practices that result in loss of third-country markets for U.S. exporters and practices that result in diversion of imports to U.S. markets.

As you know, the current version of section 301 includes a broad definition of unfair practices, including actions that are "unjustifiable, unreasonable, or discriminatory" burdens on U.S. commerce. Conceivably, this definition could encompass the practices you propose to specify in the statute. It is true, however, that section 301 has not been interpreted very broadly since its enactment in 1974. Therefore, adding these new causes of action could result in more cases filed by private parties and possibly to a greater willingness by presidents to take action against foreign targeting practices.

One reason that the statute has not been used very often is the problem of finding some form of retaliation that is both credible to the foreign government and acceptable to affected U.S. interests. Thus, adding new causes of action would be an improvement, but the difficulties of threatening retaliation in order to encourage the removal of the unfair act would remain.

Senator **Mitchell**. I thank you, Mr. Chairman.

The **Chairman**. Where are we on the rounds of questions?

Senator **Mitchell**. Senator Bradley is next.

The **Chairman**. Is Senator Bradley next?

Senator **Bradley**. Yes; I would be very brief, Senator. I know you want to move on.

You have in your testimony talked about long-term steps we could take to get the value of the dollar down. I wonder if you have in mind any possible short-term steps that we could take to get the value of the dollar down. In particular, are you supportive of a policy of intervention in foreign exchange markets?

Dr. **Stern**. I'm supportive of the intervention that is going on now, and I think it should be understood that you have to, eventually make it long term. We have to address the macroeconomic policies that have brought the dollar to the value at which it is and coordinate of our macro policies with those of our major trading partners.

Senator **Bradley**. Are you supportive of intervention policies that would be unsterilized as well as sterilized? Or is that out of your purview?

Dr. **Stern**. Well, it's out of my purview. I mean you are asking my personal opinion on all of these questions.

I think you have got to have it signaled to help the whole economy. I think you have to get that kind of cooperation from the Fed.

Senator **Bradley**. Do you have an opinion?

Dr. **Norwood**. No.

Senator **Bradley**. Thank you very much.

The **Chairman**. Any other questions?

Senator **Baucus**. One very brief point. This would follow up on your point, Mr. Chairman, with respect to the study before the ITC on the competitiveness and caused by our tax bill.

I hope that the ITC looks at our request not from the point of view of the degree to which various provisions of Treasury II have a revenue effect on various industries. That's not the point of this. Treasury has already done its study of the revenue effect.

Dr. **Stern**. Exactly. And we will be using that methodologically as an input to——

Senator **Baucus**. Rather, the purpose of the study is to determine the degree to which Treasury II affects the competitive position of various industries; not the revenue effect of various industries.

Thank you.

The **Chairman**. Let me second that. We have not only Treasury's estimates, we have everybody else's who doesn't like Treasury's estimate on the revenue estimates.

Thank you very much, both of you.

Now if we can move to Owen Bieber, the vice president of the American Federation of Labor and the president of the United Automobile Workers.

Now we will ask all of the witnesses to limit their remarks to 5 minutes. Their statements will be in the record in full. And as you can tell from the first two witnesses, we have ample questions for everybody.

Mr. Bieber, go right ahead. I see you have Mr. Warden with you.

STATEMENT OF OWEN BIEBER, VICE PRESIDENT, AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS; AND PRESIDENT, INTERNATIONAL UNION, UNITED AUTOMOBILE, AEROSPACE AND AGRICULTURAL IMPLEMENT WORKERS OF AMERICA, DETROIT, MI, ACCOMPANIED BY: MR. DICK WARDEN, LEGISLATIVE DIRECTOR, UNITED AUTOMOBILE, AEROSPACE AND AGRICULTURAL IMPLEMENT WORKERS OF AMERICA

Mr. BIEBER. Thank you, Mr. Chairman. I'm not sure I can quite make that 5 minutes, but I will try to be as brief as I can.

We have submitted a detailed statement to you and to the members of the committee. What I would like to do is try to condense quickly some of the important points as we see them in that statement.

I am the president of the United Auto Workers and a vice president of the AFL–CIO, and I, of course, want to thank you, Mr. Chairman, and the members of this committee, for giving us the opportunity to share our views on trade policy with you. And in addition to the statement, I have appended to that statement a copy of the resolution on international trade and investment adopted in October of this year by the 16th AFL–CIO convention.

For several years now, we in the labor movement have tried to convince Members of Congress and policymakers in the administration of the need to develop our own long-term trade policy in the interest of the American people.

The sad fact is that we do not have such a policy. Its absence has meant that we are taken advantage of by others who want to exploit our markets. And we merely react usually, unfortunately, I have to say, ineffectively to their policies. We think it's time for us to call the shots for ourselves.

Now with the trade deficit at a level that can only be described as an emergency, there does appear to be a much greater recognition here on Capitol Hill and even by some in the administration that free trade is an economist's concept rather than a real-world practice. It has not been and cannot be acceptable as national policy.

In the years past when trade was a relatively small part of our economy, the Government's indifference toward unfair trade practices of other nations and ineffectiveness in negotiations concerning them was understandable. Similarly, the Government's response to industries hurt by fair trade was slow and unsuccessful in preventing long-term injury to domestic production and employment. Today, there is no excuse for the continuation of this measured response to the trade problems of our industries.

In the domestic auto industry, for example, the most serious trade problem in recent years has been the enormous increase in the number of motor vehicles and automotive components exported to this country from Japan. Until the late 1960's, Japan severely restricted imports and local production of cars or investment in Japanese firms by foreigners. When Japanese production and sales were relatively small, these restrictions were a minor irritant to the U.S. firms and of no particular concern to the U.S. Government. However, by 1967, Japan had become the second largest auto-producing nation in the world, and these restrictions had grown in importance. The Japanese removed the investment restrictions soon thereafter, but by this time the opportunity for U.S. firms to export in large volume or build capacity in Japan had been lost. Unfair restrictions on U.S. exports of cars remained in place and continue today despite many years of negotiations over their removal.

In 1988, when the output of new auto-exporting nations joins the unrestrained exports of Japan and Europe, the U.S. industry will face an even greater and deeper crisis. Stimulated by unfair trade practices in Mexico and Brazil, and by incredibly low wage rates in South Korea, resulting from the lack of basic worker rights, imports from these countries will be available in large numbers in this country.

The so-called transplant vehicles produced in the U.S. plants of foreign companies or joint ventures of foreign and U.S. firms will also be a source of continuous concern so long as they have much less U.S. content than other domestically produced cars.

The UAW conservatively estimates the combination of these forces will reduce auto industry employment in this country by about 25 percent before the end of this decade, eliminating hundreds of thousands of jobs that pay decent wages. The estimates of the U.S. Department of Commerce confirm those of our economists. We do not believe we are overstating the gravity of the immediate crisis facing our industrial base and the workers and companies dependent upon it.

The proliferation of unfair trade practices around the globe, as shown by the size of the Annual Report on National Trade Estimates just completed, and their impact on U.S. trade, has made bilateral negotiations over individual practices unworkable. We need an overall approach which gets the high-level attention of both our Government and the governments of our trading partners.

The UAW has supported the Trade Emergency and Export Promotion Act, S. 1449, as a vehicle for addressing this type of problem. This bill would impose penalties on countries which do not eliminate their excessive trade surpluses with the U.S. only if they fail to remove their unfair trade practices.

S. 1449 proposes a surcharge on such imports. The sanction could be an embargo, quota, or another penalty and still be effective. Strong measures such as this must be pursued by the U.S. if progress is to be made in eliminating these practices and reducing the size of our trade deficit.

There are many foreign practices not considered unfair under current laws, but we believe they are. One of these is the abuse of the basic rights of workers. Such as basic rights to free association, to organize and bargain with employers, to standards for minimum wages, hours of work, occupational safety and health, to the prohibition of forced labor and a minimum age for employment, have been included in the U.S. law governing preferential treatment of imports from developing countries under the generalized system of preferences.

Further recognition of the unfairness of denial of these rights under our trade laws is needed. While low wage rates, in themselves, can not be defined as unfair, the maintenance of such wages through repressive government action in the workplace should be defined as a subsidy for goods produced under these conditions which are exported to the United States.

The **Chairman**. Have to ask you to conclude, Mr. Bieber.

Mr. **Bieber**. If I can have about 1 more minute, I can do it.

The **Chairman**. OK.

Mr. **Bieber**. We believe that the industrial base of our Nation and the standard of living of its citizens cannot easily bear a decay of these proportions in the domestic auto-related industries. The implications of this steep drop in domestic employment for other large manufacturing industries should be reason for great concern for all of us; for those of you with such industries in your States and for representatives of workers in these industries.

The specific measures required to meet the challenge may vary from industry to industry. Our Government must be ready to negotiate restraint with foreign governments which are the source of injury or potential injury to U.S. production. At the same time, commitments to invest in the industry must be obtained from domestic producers.

Mr. Chairman, we appreciate this opportunity to discuss our views on the critical import issues you have under consideration before your committee.

[The written statement of Mr. Bieber follows:]

SUMMARY
STATEMENT OF
OWEN BIEBER, PRESIDENT
INTERNATIONAL UNION, UNITED AUTOMOBILE, AEROSPACE AND AGRICULTURAL IMPLEMENT WORKERS OF AMERICA (UAW), and VICE PRESIDENT, AFL-CIO

before the

SENATE COMMITTEE ON FINANCE

on the subject of

TRADE POLICY

NOVEMBER 20, 1985

Mr. Chairman, my name is Owen Bieber. I am the President of the United Automobile, Aerospace and Agricultural Implement Workers of America (UAW) and a Vice President of the AFL-CIO. I wish to thank you for the opportunity to share our views on trade policy with you and the Members of the Committee on Finance. Appended to our prepared statement is a copy of the Resolution on International Trade and Investment adopted in October, 1985 by the 16th AFL-CIO Convention.

For several years now, we in the labor movement have tried to convince Members of Congress and policy-makers in the Administration of the need to develop our own long-term trade policy in the interests of the American people. The sad fact is that we do not have such a policy. Its absence has meant that we are taken advantage of by others who want to exploit our markets; we merely react, usually ineffectively, to their policies. It's time for us to call the shots for ourselves.

Now, with the trade deficit at a level that can only be described as an emergency, there appears to be much greater recognition on Capitol Hill, and even by some in the Administration, that "free trade" is an economists' concept, rather than a real world practice. It has not been, and cannot be, acceptable as national policy.

In years past, when trade was a relatively small part of our economy, the government's indifference toward unfair trade practices of other nations and ineffectiveness in negotiations concerning them was understandable. Similarly, the government's response to industries hurt by fair trade was slow and unsuccessful in preventing long-term injury to domestic production and employment. Today, there is no excuse for the continuation of this measured response to the trade problems of our industries.

In the domestic auto industry, for example, the most serious trade problem in recent years has been the enormous increase in the number of motor vehicles and automotive components exported to this country from Japan. Until the late 1960's, Japan severely restricted imports and local production of cars or investment in Japanese firms by foreigners. When Japanese production and sales were relatively small, these restrictions were a minor irritant to U.S. firms and of no particular concern to the U.S. government. However, by 1967, Japan had become the second largest auto-producing nation in the world, and these restrictions had grown in importance. The Japanese removed the investment restrictions soon thereafter. But by this time, the opportunity for U.S. firms to export in large volume or build capacity in Japan had been lost. Unfair restrictions on U.S. exports of cars remained in place, and continue today, despite many years of negotiation over their removal.

In 1988, when the output of new auto-exporting nations joins the unrestrained exports of Japan and Europe, the U.S. industry will face an even deeper crisis. Stimulated by unfair trade practices in Mexico and Brazil, and by incredibly low wage rates in South Korea, resulting from the lack of basic worker rights, imports from these countries will be available in large numbers in this country. The so-called "transplant" vehicles, produced in the U.S. plants of foreign companies or joint ventures of foreign and U.S. firms, will also be a source of continuous concern so long as they have much less U.S.-content than other domestically produced cars. The UAW conservatively estimates the combination of these forces will reduce auto industry employment in this country by about 25 percent before the end of this decade, eliminating hundreds of thousands of jobs that pay decent wages. The estimates of the U.S. Department of Commerce confirm those of our economists. We do not believe we are overstating the gravity of the immediate crisis facing our industrial base and the workers and communities dependent upon it.

The proliferation of unfair trade practices around the globe, as shown by the size of the Annual Report on National Trade Estimates just completed, and their impact on U.S. trade, has made bilateral negotiations over individual practices unworkable. We need an overall approach which gets the high-level attention of both our government and the governments of our trading partners. The UAW has supported the Trade Emergency and Export Promotion Act, S. 1449, as a vehicle for addressing this type of problem. This bill would impose penalties on countries which do not eliminate their excessive trade surpluses with the U.S. only if they fail to remove their unfair trade practices. S. 1449 proposes a surcharge on such imports. The sanction could be an embargo, quota, or another penalty and still be effective. Strong measures such as this must be pursued by the U.S. if progress is to be made in eliminating these practices and reducing the size of our trade deficit.

There are many foreign practices not considered "unfair" under current laws, but we believe they are. One of these is the abuse of the basic rights of workers. Such basic rights — to free association, to organize and bargain with employers, to standards for minimum wages, hours of work, occupational safety and health, to the prohibition of forced labor and a minimum age for employment — have been included in the U.S. law governing preferential treatment of imports from developing countries under the Generalized System of Preferences. Further recognition of the unfairness of denial of these rights under our trade laws is needed. While low wage rates, in themselves, cannot be defined as "unfair", the maintenance of such wages through repressive government action in the workplace should be defined as a subsidy for goods produced under these conditions which are exported to the U.S.

We believe that the industrial base of our nation and the standard of living of its citizens cannot easily bear a decay of these proportions in the domestic auto and related industries. The implications of this steep drop in domestic employment for other large manufacturing industries should be reason for great concern for all of us — for those of you with such industries in your states and for representatives of workers in these industries. There are many industries now, and there will certainly be more, subject to the same type of attack from imports produced under both fair and unfair conditions. We need these manufacturing jobs to keep our economy strong, our workers employed and our living standards high. The elimination of unfair trade practices, though important, will not alone prevent job losses. Other measures are needed. We need a trade policy which can effectively protect workers from worldwide transfers of capital and advanced technology. The constant search for low-cost production can only impoverish the American economy unless our government is willing to defend this market as other governments around the world defend their markets. The specific measures required to meet this challenge may vary from industry to industry. Our government must be ready to negotiate restraint with foreign governments which are the source of injury or potential injury to U.S. production. At the same time, commitments to investment in the industry must be obtained from domestic producers.

Mr. Chairman, we have appreciated this opportunity to discuss our views on the critically important issues you have under consideration. Thank you.

opeiu494

STATEMENT OF
OWEN BIEBER, PRESIDENT
INTERNATIONAL UNION, UNITED AUTOMOBILE, AEROSPACE AND AGRICULTURAL IMPLEMENT WORKERS OF AMERICA (UAW), and
VICE PRESIDENT, AFL-CIO

before the
SENATE COMMITTEE ON FINANCE
on the subject of
TRADE POLICY
NOVEMBER 20, 1985

Mr. Chairman, my name is Owen Bieber. I am the President of the United Automobile, Aerospace and Agricultural Implement Workers of America (UAW) and a Vice President of the AFL-CIO. I wish to thank you for the opportunity to share our views on trade policy with you and the Members of the Committee on Finance.

The labor movement shares the belief of many Americans that the U.S. trade deficit constitutes a national emergency. There is no way we can afford the current imbalance in our trade relationships. The trade deficit is getting worse, not better. The burgeoning trade deficit is but a symptom, though, of what ails the U.S. economy. The lack of political commitment to a national trade policy which works for Americans allowed this situation to develop. Without our own trade policy, we have been forced to react to the policies of others. It is time for us to call the shots for ourselves.

It is argued that, since the end of World War II, we have had a trade policy — "free trade"— which operates in the best interests of our citizens, but "free trade" hardly describes the policies of the nations of the world. For nearly two decades, this approach seemed to be satisfactory because of the relatively minor impact of trade on our economy and the continuing weakness due to wartime devastation of both our former allies and adversaries alike. This situation could not, and did not, continue. Since the mid-1960's, the economic fortunes of the U.S. have been increasingly affected by the trade policies of other nations.

Rather than critically assess the impact of the growth of serious foreign economic competitors, our government continued to espouse and practice a policy of "free trade" while nearly all other developed nations maintained a variety of policies aimed both at limiting imports and encouraging exports. These fell into both the "fair" and "unfair" categories under our laws. U.S. firms made their own peace with these policies by investing in those countries which would allow it, producing for the market there and exporting to the U.S. and to other countries formerly served by U.S. exports. They even took their advanced technology with them when setting up these plants. Japan, however, either limited or barred U.S. investments in many key industries during this period, encouraging foreign firms to license technology to its own companies. During these years, the dollar was overvalued because of its role as the major reserve currency in a system of fixed exchange rates and the confidence of other countries in the strength of the U.S. economy, giving further incentive for U.S. firms to favor foreign investment to meet overseas demand. Even U.S. tax law favored foreign investment by granting special status to profits earned abroad and foreign taxes paid.

During recent decades, the U.S. has maintained an open market for the output of industries developed abroad to compete with our once dominant producers. Contributing to this competition are the American-based firms which joined the ranks of the "foreign producers" through wholly owned subsidiaries or joint ventures with companies abroad, adding to U.S. imports and replacing U.S. exports to other countries. U.S. multinational firms displayed little loyalty to their workers in the U.S. or the communities where they had become important sources of stability. Japanese firms, using acquired technology, a protected home market and a relatively low-paid workforce, have become internationally competitive in industry after industry in manufacturing. These firms and their competitors have transformed the world economy in the past 20 years and, with it, the status of the U.S. as the world's foremost manufacturing nation.

In 1985, there are hardly any industries in which American producers are free from tough international competition. Competitors in Europe, Canada and Japan are formidable in many areas of production, including those relying upon advanced technology. In addition, these developed countries have been joined by newly industrialized countries (NIC's), such as Taiwan, South Korea, Singapore, Hong Kong, Mexico and Brazil, among others. All of these nations, individually or through associations like the European Economic Community, have used government policies to help develop new industries, protect such industries while they are young, encourage their exports, limit imports of competing goods and, generally, assist in pursuing economic development strategies. There have been many unfair trade practices which contributed to this growing competition. The lack of priority given to trade problems by the government encouraged affected U.S. companies to accomodate to these practices rather than fighting them.

Some basic industries in the U.S were initially too strong, or their market too different from those abroad, to be subject to effective competition from imports. In the auto industry, for example, despite the investment of U.S. producers around the world to jump over barriers to U.S. exports, which began shortly after the turn of the century, imports have become a serious problem only in the past decade. The problem began with the oil crisis of 1973-74 which transformed U.S. demand for cars to more closely resemble the market in Europe and Japan. The demand for small, fuel efficient cars increased as a share of total sales.

In the last 20 years we have completed two rounds of multilateral trade talks intended to move all nations closer to the practice of free trade. Instead, the multilateral agreements have shifted the emphasis in protection of industries from tariffs to non-tariff barriers, of which there are an infinite variety. The attempt to deal with these newer barriers in the 1979 Tokyo Round of negotiations was frustrating for many of those involved and results have been modest. In the end, there has been no dramatic reduction in the barriers set up by our major trading partners. The size of the Annual Report on National Trade Estimates indicates this lack of progress.

Just as in the early post-war period, in 1985, the dollar is highly overvalued relative to the currencies of our major trading partners. This provides an incentive for U.S. firms to increase foreign investments (made cheap by the currency misaligment) and substitute local production for U.S. exports and imports for U.S. production. The longer the currencies remain misaligned, the larger the impact on the U.S.

This combination of developments — the continued U.S. commitment to "free trade" as an adequate policy, the overvalued dollar and the proliferation of sophisticated competitors in a constantly expanding range of products and services — has produced what cannot be described as anything other than an emergency for our nation. It is a situation which cannot be wished away by calls to convene another round of multilateral negotiations as the Administration has done; it will not disappear because of "messages" sent to our trading partners by the Congress. In 1985, unlike 20 years ago, our trade problem is not a small part of the U.S. economy and it does not affect just a few, isolated industries.

The trade crisis we face is massive, with a merchandise deficit in the range of $150 billion expected for 1985. The much higher volume of world trade and international financial transactions and the links with the economies of other countries forged by U.S. companies operating in Europe, Japan, Canada and the developing countries make the U.S. trade emergency an international problem in which all Americans have an important stake.

The emergency was not created overnight. As we have indicated, problems did not just begin to appear with OPEC and with the oil crises of 1973 and 1979, or the run-up of the dollar beginning in 1980, or the debt problems of developing countries, or the slow growth of the world economy in the 1980's. All these factors have contributed to the timing of the emergency but solving each of those problems, and eliminating all identifiable unfair trade practices still would not undo the fundamental changes in the international distribution of production and employment which threaten to reverse the economic gains achieved in recent decades for American industry, its workers and the communities in which they live.

In the auto industry, we have watched problems broaden and deepen in the past 10 years as auto markets in developed countries have become more similar and developing countries have increasingly forced their integration into the industry's international structure. The same, or similar models are made and sold in many national markets by multinational producers. Parts are supplied from, and assembly takes place in, Mexico, Brazil, Korea, Taiwan, Malaysia and other developing nations.

Efforts to preserve domestic production of automobiles since 1979 give an indication of how inadequately trade policy has been handled by our government and how U.S. industries can be devastated by "fair" trade which was nurtured and supported by "unfair" trade. When the second oil crisis hit in 1979, sending gasoline prices sky high, demand for small, high mileage cars took off as well. Because of insufficient domestic capacity in this segment, the demand for imports increased — their share of total sales jumped from an already high 17.9 percent in 1978 to 26.7 percent in 1980. The impact of the oil price increase on all manufacturing industries was powerful and on auto production it was tremendous. Total auto sales fell, and domestic production and employment plunged even faster, each year from 1979 to 1982.

In the wake of the domestic auto industry's 1979 collapse, the UAW filed a petition for relief under Section 201 of the Trade Act of 1974. This section covers industries suffering injury from "fair" imports and allows tariff and/or quota relief. The International Trade Commission ruled against us by a 3-2 margin. The Commission recognized that imports were, indeed, a cause of injury to the industry, but found that the decline in total sales caused more injury. While we believe the ITC conclusion was wrong, it is important to recognize that the U.S. injury test is more stringent than the one required by the GATT.

The unfavorable ITC ruling contributed to a flurry of activity in Congress to limit Japanese auto exports to a maximum of 1.6 million per year for at least three years as a way of providing time for the domestic industry to become competitive in small car production. The reaction in Congress to this decision encouraged the new Reagan Administration to begin talks with the Japanese aimed at limiting their auto exports to this country. These talks concluded in May, 1981 with a voluntary restraint agreement (VRA) to limit exports to 1.68 million for the year ending March 31, 1982 and unspecified equal or higher limits in the following two years depending upon market conditions. Virtually all other major industrial nations already had much tighter restrictions against Japanese imports. Imports of Japanese cars have been held to a 3 percent share of the market in France and 10 percent in West Germany.

The agreement limited only Japanese imports of cars, not trucks or parts, and made no demands upon American firms to commit financial resources to competitive small car production. The fact that the U.S. government took any action at all indicated its recognition of the extremely weak condition of an industry of central importance to the U.S. economy and that the stiffest competition was coming from a country which not only shielded its own market from our exports but had also prevented investments in its auto firms by our producers until Japan had become the world's second largest auto producer. Despite the obvious injury to the industry, the Administration acted only because of strong congressional pressure.

The UAW recognized that, while this agreement was of decisive importance in limiting the impact of imports on auto employment and production, it was not enough to assure that U.S. facilities would emerge at the end of the restraint period internationally competitive in all auto markets, including the large market for small cars. Thus, even with the VRA, domestic output plummeted. For 1981, imports continued to increase their share of auto sales, accounting for 27.3 percent of cars and 19.8 percent of trucks, while domestic output fell to new depths. Unemployment among workers in the auto industry hovered at about 25 percent, as employment by auto and truck producers dropped by 250,000 and by the industry's suppliers an additional 500,000. The midwest section of the U.S., where production is concentrated was in an economic depression.

In December 1981, the proposed Fair Practices in Automotive Products Act was introduced to address the problems left untouched by the VRA. The legislation would have required the domestic content of cars sold by each company to increase with the volume of its U.S. sales. This requirement would apply to all companies equally, domestic or foreign-based. It would result in U.S. investment by firms with large U.S. sales and profits while maintaining high domestic content by existing U.S. producers to insure stability in parts production and employment. This is the type of government policy we believed then, and still believe, is needed when an important U.S. industry is threatened by imports which are not aided by recognized unfair practices. Despite passage of that legislation by the House of Representatives in 1982 and 1983, it unfortunately never came to a vote in the Senate and never came into play as a standard for fair trade in the auto industry.

With U.S. policymakers thus satisfied with only the VRA with Japan as the U.S. auto trade policy, we can look at the impact of this restraint from 1981-1984 and its extension to March 31, 1985 at the 10 percent higher level of 1.85 million vehicles.

The restraints on Japanese imports provided some stability in the industry, allowing U.S. firms to make important progress toward competitiveness. This occurred even though the most meaningful benefit of the VRA was only felt in the past two years, as the economy recovered from the 1980-82 recession. Large capital investments were made and research and development spending has grown in both dollar value and as a proportion of sales.

The impact of this commitment of investment in the auto industry also directly affects many other capital goods industries which are leaders in advanced technology and subject to intense international competition. The auto industry is a major consumer of computer-aided design equipment, industrial robots, machine tools and electronics as well as the products of other important industries, such as steel, rubber, glass and textiles which are struggling to improve their competitiveness. The size of the market provided by the auto industry for such products stimulates innovations in this wide range of industries which represent a large part of our economy's industrial base. The stability in the auto market established by the VRA made new investments and R&D spending possible in other industries as well.

The VRA helped in meeting its objectives while keeping car price increases modest. In subcompact cars, the market segment most affected by the VRA, price increases of U.S. cars have been quite low. The Bureau of Labor Statistics measure of new car prices rose less than the overall Consumer Price Index for the VRA period.

While the industry has made progress, serious problems remain. One of the foremost of these is the dollar-yen exchange rate. This problem, of course, also plagues all U.S. industries competing with Japan. From 1981 until as recently as September, the 25 percent appreciation in the value of the dollar gave Japanese cars a tremendous cost advantage and overcame the many cost reduction and efficiency promoting programs of U.S. auto makers. The 1984 U.S. deficit with Japan in autos was a staggering $20 billion. We expect this to grow by $5-$7 billion for all of this year because of the absence of restraints and the imbalance in exchange rates. The VRA was never intended to address this type of ongoing inequity, yet to have lifted it while the exchange rate inequity remained, exposed the industry to a disadvantage it could not counter on its own.

Our deficit with Japan was a huge $37 billion in 1984. It may reach $50 billion in 1985, despite repeated efforts to open export opportunities there. The endless hours of negotiations with Japan from 1980 to 1984 resulted in an increase in our exports from $21 billion to only $24 billion. All of this gain and more will be wiped out by the 1985 increase in Japanese car exports to this country.

The lifting of the VRA produced another inequity. The U.S.-based auto makers are abandoning domestic production of small cars in their own plants. GM has plans to import cars from Japan and Korea. These will be "captive imports", vehicles produced abroad and imported by U.S. manufacturers to be sold under their nameplate through their own dealer networks. Combined with the subcompacts produced by its joint venture with Toyota in Fremont, California, they add up to more small cars than GM has ever sold in a year. Even with the Saturn project commitment, GM will have become one of America's largest importers. Ford and Chrysler are increasing their own captive imports to compete. The failure of the Administration to devise an effective trade policy for the auto industry is in large part responsible for the industry pursuing this plan.

The ultimate failure of the VRA in auto to stabilize employment and production, especially in the small car-segment, was due to its covering too short a period of time to convince U.S. producers of the need to make additional investments and its lack of recognition of the increasing internationalization of parts production. With a product cycle of about seven years and product development time of up to five years, the companies saw the VRA as only a temporary policy. They used their at first limited and later (1983-85) enlarged, financial resources to shore up their more profitable larger models to protect them from potential competition - rather than updating their less profitable small cars.

While imports in the 1979-84 period caused a significant loss of U.S. production and many lost jobs for workers, we believe that this period's difficulties will be overshadowed by the increase in imports from now to 1990. The plans of GM, Ford and Chrysler to import cars and purchase others made by joint ventures or foreign companies in the U.S. with a relatively large proportion of imported parts, will lead to reduced U.S. production and fewer jobs for American workers even if total U.S. sales grow. The UAW has made projections for 1988 which show how serious the auto industry's employment situation will be. We expect imports from Japan for sale by Japanese companies to increase from 1.7 million in 1984 to 2.6 million in 1988. Imports from Japan for sale by U.S. auto companies will grow from only 100,000 in 1984 to 500,000 in 1988 if only the already announced plans are carried out. European imports are expected to remain constant at 500,000, except for the increase of 100,000 cars imported by Ford for its own sales. By 1988, there will be new sources of significant imports. Plans of Ford and GM to bring cars in from Korea will add 200,000 and Ford and Chrysler will import 160,000 from Mexico. In addition, Hyundai, which began selling cars in Canada last year, should add 230,000. With these quite conservative assumptions, the total number of imported cars in 1988 comes to 4.3 million, of which nearly one million will be sold by U.S. companies. This compares with total 1984 imports of 2.4 million in 1984. The total increase in imports would, then, be 80 percent.

The UAW welcomes, but is also concerned by the growth of so-called "transplant vehicle" production in the U.S. These cars are made here by foreign companies, or by joint ventures of foreign and U.S. firms. Plants now in operation turned out 370,000 cars in 1984. These three operations will grow to at least eight in 1988, producing 1.4 million cars. Our current experience with these plants, and the announcements made by the companies involved, lead us to believe that a large proportion of the total value of these cars will be imported from Japan, Mexico and other countries. The value of U.S. production and labor in these vehicles will only add up to 30-40 percent of the total. In terms of generating employment for Americans, these vehicles are not in the same league as the over 90 percent U.S. content cars now made by the U.S. companies.

If we assume a strong auto market of 11.2 million sales in 1988, we have projected that it will be met by 4.3 million imports and 1.4 million transplants, leaving room for 5.5 million fully domestic car sales. In 1984, sales of such high U.S. content domestic cars were 7.6 million. The total impact of this shift to imports and imported major components, plus assumed productivity growth of 5 percent per year, would be a decline of about 25 percent in U.S. auto employment. The fully assembled import share would be 33 percent, compared to 23.5 percent in 1984.

We believe these assumptions about the growth in import share are conservative. There is a considerable potential for even greater import penetration, both from captive imports of the U.S. companies and imports from foreign producers. Anyone who thinks our projections are too pessimistic need only consult the study of the U.S. Department of Commerce from April, 1985 which estimated a 36 percent import share and 4.0 million imports in 1988. We in the UAW are hardly alone in our concern that the auto industry is on the verge of unprecedented import competition and employment losses. The plans of GM, Ford and Chrysler to dramatically expand their own imports are a blow to our members and to the companies' domestic suppliers, which have little chance of making sales to the foreign makers of small cars. This situation could have been avoided if our government had developed an appropriate response to the problem caused by "fair" imports back in 1981.

While this problem for the auto industry remains, the UAW has large numbers of members in other industries who have been hurt by ineffective trade policies. Not only increasing imports, but foreign restraints on our exports have cost jobs in the aerospace, agricultural implement and construction machinery industries.

Significant unfair restrictions on U.S. exports have hurt our exports of aircraft and auto parts, especially in Latin America. At the same time, growing imports from subsidiaries and licensees of U.S. companies are adding to imports from foreign companies in the construction and agricultural machinery industries. Exports of construction machinery have dropped from over 40 percent of industry shipments in 1982 to 20 percent in 1984. The spread of co-production agreements in the aerospace industry doubled the foreign content of U.S.-built aircraft from 1978 to 1983, and the trend is continuing. In many cases, though, the threat of lost markets and the appeal of special concessions from host governments and reduced costs convinced companies to accede to the policy goals which were the reason behind these unfair practices. Actions must be taken to promote our exports in many industries and in agriculture.

We have considered a variety of proposals, and the one which addresses most of our concerns and is the best available approach to counter the impact of unfair trade practices is the proposed Trade Emergency and Export Promotion Act (S. 1449). This bill takes note of the failure of the Executive Branch of our government to pursue our rights under the GATT to contest unfair trade practices abroad.

The focus of S. 1449 is on removing the unfair practices of some of our largest trading partners. It prevents the U.S. trade deficit with these trading partners from continuing to grow while their barriers remain in place. Under the bill, each country with an excessive non-petroleum trade imbalance with the U.S. would be assessed a 25 percent surcharge on its exports to the U.S. if its trade surplus does not fall by a specified amount. We can no longer accept the unending negotiations to remove unfair barriers to our exports, one by one, while the trade deficit undermines our industrial base. The Administration's inaction is inexcusable and the recent initiation of a few cases under Section 301 of our trade law is in no way an adequate response. In the past, we have negotiated with these countries over their unfair practices for years on end with only minimal success and little or no impact on trade. The surcharges imposed would be interim measures pending the removal of the unfair practices.

We believe that it is absolutely essential for the U.S. government to take effective action to control the trade deficit. The already dangerous 1984 deficit of $123 billion is headed to $150 billion this year. Our trade balance in manufactured goods has shifted from a surplus of $12.5 billion in 1980 to a deficit of $88.7 billion in 1984 and it is still getting worse. Our exports have barely changed over this period, while imports soared by $100 billion. This has led to serious trade problems for an ever growing number of manufacturing industries, even those counted among our most technologically advanced: semiconductors, telecommunications, computer equipment, chemicals and others. In fact, the U.S. trade surplus in high technology manufactured goods fell from $26.6 billion in 1980 to only $6.2 billion in 1984. Of this $20 billion decline, Japan has accounted for $12.1 billion and Brazil, Taiwan, South Korea, Hong Kong and Singapore together were responsible for $5.4 billion.

We in the UAW are also deeply concerned by the labor policies of the government's in South Korea, Taiwan and other developing countries which contribute to their undercutting U.S. workers. In these countries, repression of trade unions is often a central part of export promotion programs and efforts to attract investment by multinational producers. Workers are not afforded the internationally recognized worker rights of freedom of association and the right to organize and bargain with employers. The AFL-CIO, IUE, UAW and others recently testified that the labor practices of many countries constitute an unfair trade practice in hearings before an interagency staff committee on administration of the Generalized System of Preferences. The workers there have been prevented from obtaining a fair share of the wealth generated by large trade surpluses because of direct and indirect government repression. Lifting the constraints on worker rights in these countries would encourage the growth of their domestic markets. This would reduce the pressure to export and possibly open up opportunities for U.S. exporters. This is one area in which the definition of unfair trade should be expanded.

The suppression of basic labor rights should be treated under U.S. law and in international trade agreements as a subsidy subject to countervailing actions when imports which benefit from these abuses injure, or threaten to injure, a U.S. industry.

While there is still much work to be done in clarifying the distinctions between fair and unfair trade, there can be no doubt the American industries will be under intense pressure from both. The experience of the auto industry in seeking relief under Section 201 of our trade law makes clear that our current trade policy toward injury caused by "fair" imports is not adequate. We believe the number of these cases will be growing in the future as multinational firms, using advanced technology and equipment developed in their home market, seek out the lowest-cost location of production. A small but important step in responding to the problems of U.S. industries would be to change the injury test in Section 201 to the GATT standard from its current more stringent standard.

The remedies fashioned by our trade laws and policies must prevent serious injury to our important manufacturing industries through negotiations with our trading partners. U.S. trade policy must promote government actions which establish a stable domestic market and make investment in the U.S. desirable. At the same time, we cannot leave the actual decisions to invest solely to the firms in the industry. Our government's actions in defending our market must be conditioned on continued production and new investment by domestic producers.

In the area of unfair trade practices, the definition of such practices must be expanded and our trade policy must become more active. The U.S. can no longer afford to respond at a measured pace to unfair practices. Our government must be ready to negotiate forcefully over the variety of practices which hurt our industries and set firm time limits on these talks. The threat of retaliation must be real if we are to make progress in eliminating these practices.

Mr. Chairman, we have appreciated this opportunity to discuss our views on the critically important issues you have under consideration. Thank you.

opeiu494

Resolution Adopted by the 16th Constitutional Convention of the AFL-CIO

October, 1985

International Trade and Investment

The goal of U.S. trade policy must be the attainment of a fair trading environment that allows this nation to be an advanced and diversified economy, promoting full employment and rising living standards.

Fair trade means that the inequities present in the international trading system must be rectified and due regard given to domestic interests in both the national and international initiatives of U.S. trade and investment policy.

The United States must retain its manufacturing, agricultural, and maritime industries. The nation's foreign trade policy must promote—not undermine—this goal.

Immediate action in the form of quotas and/or tariff increases is needed to reverse the disastrous decline in America's trade account. These measures should be targeted at those countries that maintain large and unreasonable trade surpluses with the United States. No nation can sustain indefinitely the massive deficits now confronting the United States.

U.S. trade law and policy must be brought into line with today's trade realities. The academic abstractions of free trade and natural comparative advantage, if they ever had any relevance, are inadequate guides for the real world of international commerce in the 1980s. U.S. trade law must be modernized to reflect contemporary realities in a world where the United States is the only country which exposes its industrial foundation to unlimited erosion from imports.

The overhaul of U.S. trade law needed to remedy general shortcomings must include:

- Relief from injury due to unfair trade practices such as dumping, subsidies, and disruptive imports from nonmarket economies. At present, too many of the injurious practices developed in recent years escape U.S. law against unfair trade practices, and other countries can increase their unfair sales in this country without fear of penalties.
- Relief from export-oriented industrial targeting practiced by foreign governments that seek to expand their sales and employment at the expense of the United States or other countries. U.S. laws designed long before these practices developed should be amended to provide effective relief.
- The U.S. standard for import relief in the "escape clause" (Section 201 of the Trade Act) should be eased, specifically recognizing plant closings and layoffs as signs of serious injury in qualifying for relief. Providing relief to U.S. industries injured by imports is a right recognized under international law, but the U.S. standards for qualifying for such relief are stiffer than international rules require.

Beyond general reform of existing trade law, difficulties encountered by individual industries require remedies tailored to their own special circumstances.

To assure that the U.S. remains a producer of automobiles and other key products, including parts, the enactment of domestic content laws continues to be needed. Corporations that have benefited from access to U.S. markets should be required to maintain a fair share of production in the United States providing jobs for American workers.

The President's national policy for import restraints on steel must be fully implemented, and the Steel Import Stabilization Act must be vigorously enforced, particularly with respect to modernization and the training of displaced workers. Should the import restraint program prove ineffective, quota legislation will be necessary.

The President must immediately implement the congressional direction to negotiate voluntary production restraints on copper. If congressional intent is ignored, legislation will be necessary to maintain a vigorous domestic industry.

Despite the theoretical safeguards contained in the Multi-Fiber Arrangement (MFA), imports of textiles and apparel have continued to increase dramatically in the last two years. The Textile and Apparel Recovery Act of 1985 is needed to make the promise of MFA a reality and to roll back imports to a reasonable and stable level.

Imports of footwear have now captured 75 percent of the domestic market. Despite recommendations from the International Trade Commission, the President denied import relief to the beleaguered shoe industry. Congressional action is urgently needed to reverse this decision.

Since the AT&T divestiture, imports of telecommunications products have inundated the American market, while foreign markets remain closed to American goods. Legislation is needed to correct this inequity and reduce the level of imported products.

Policies should be pursued to maintain and re-establish domestic electronic and television industries.

The manufacturing clause of the Copyright Law must be extended permanently to protect against widespread loss of jobs throughout the U.S. printing industry. The United States can ill afford another unilateral giveaway of U.S. production.

Policies should be enacted to assure that a significant portion of U.S. raw materials destined for export, such as grains and logs, are processed in this country.

To revive the U.S. maritime industry, legislation is needed to substantially increase the portion of cargo carried in U.S.-flag ships and to assure a strong U.S. shipbuilding base thereby enhancing national security. Further, immediate action is necessary to eliminate foreign barriers to U.S. transport carriers involved in international commerce.

The prohibition on Alaskan oil exports should be maintained, and carriage of the oil retained for U.S.-flag vessels. The U.S. merchant marine fleet should be given a more important role in providing auxiliary services for the U.S. Navy. Bilateral shipping agreements particularly for grain and coal shipments should be negotiated. The United States should ratify the UNCTAD code for liner conferences to help the domestic shipping industry attain a more equitable share of cargo generated by U.S. trade.

In addition to individual industry requirements, other trade-related measures are necessary.

The Trade Adjustment Assistance program should be restored to provide adequate compensation to those unemployed because of trade and to improve training, job search, and relocation aid for those displaced workers. Eligibility rules should be eased, to permit supplier workers and victims of foreign investments and foreign plant relocations to be covered under this program.

Export promotion is an important function of trade policy, and any program must carefully consider domestic priorities. The export of capital, technology, and price-sensitive items that damage the U.S. economy should not be promoted. The transfer of U.S. technology must be controlled to assure continued technological advances, competitive advantage for domestic production and national security. Export-Import Bank funding, including direct loan authority must be maintained in order to provide U.S. industry with tools necessary for international competition. These funds should be made available for the domestic

International Trade and Investment

purchase of U.S. products to offset foreign subsidies. Financing, however, should not be used to develop projects in other countries in industrial sectors where excess capacity exists.

Congress should not provide tariff cutting authority to the President. The few protections left to American workers and industry should be maintained.

Congress should carefully review any future bilateral free-trade agreements to assure that domestic production will be enhanced. We are especially concerned about possible developments along these lines with respect to the neighboring countries of Canada and Mexico. Simple trade liberalization will not benefit American industry and workers.

Policies must be enacted to regulate the immense flows of international investment. Current Administration emphasis on overseas investment by American firms must be redirected.

Tax loopholes and incentives for multinational companies to move abroad should be ended, the tax deferral halted, and the foreign tax credit repealed.

Items 806.30 and 807 of the tariff schedules that reduce tariffs on products containing parts produced in the United States should be repealed.

The Overseas Private Investment Corporation (OPIC), a government agency that insures private investment abroad should be terminated. OPIC is supposed to promote economic and social development in "less developed friendly countries" while furthering the balance of payments objectives of the United States. It has failed on both these counts and has contributed to the export of American jobs.

Administration support for a new international agency—the Multilateral Investment Guarantee Agency—should end. Interests of workers, both domestic and foreign, will not be furthered by providing greater protection for international business.

Recently negotiated bilateral investment treaties must be carefully reviewed to insure that protection for workers are included and domestic production not harmed.

Existing codes of conduct for multinational enterprises must be strengthened to protect the rights of workers employed by these firms and to provide effective remedies when those rights are denied.

In those countries that seek to attract industry through the exploitation of workers, international agreements are needed to improve labor standards. Provisions of the recently renewed Generalized System of Preferences concerning labor rights must be vigorously enforced, and countries that abuse worker rights should be immediately removed from the program.

The Foreign Trade Zone Act of 1938 should be repealed. Any exemption from this nation's trade laws must be proven on a case-by-case basis. At minimum, manufacturing operations should be prohibited within such zones.

The United States should end its support of loans from the Interna-

International Trade and Investment

tional Monetary Fund that require the borrowing countries to curb imports and push exports to pay their debts. In place of this approach, which has harmful repercussions on the United States and other economies, the IMF should be urged to promote balanced growth in both borrowing and lending countries.

In terms of the overvalued dollar, there must be a major effort to readjust currency values to more realistic levels and to bring some measure of stability to the exchange rate system. While national action in the form of an import surcharge is necessary to provide some immediate relief from the trade-distorting impact of the overvalued dollar, a longer-term solution must be found through coordinated international actions. The United States should undertake monetary negotiations in a variety of forums such as the International Monetary Fund (IMF), Organization for Economic Cooperation and Development (OECD), and General Agreement on Tariffs and Trade (GATT). Such negotiations should be a precondition of any multilateral trade talks. Further, the International Trade Commission should provide relief for trade injury brought about by the overvalued dollar.

The AFL-CIO shares the reservations of many at home and abroad about the appropriateness of multilateral trade negotiations. Negotiations will not implement an effective, national trade policy, correct the overvalued dollar, or reduce America's huge trade deficits. Nevertheless, if negotiations take place, the United States should focus on the following four areas:

- A principal U.S. trade negotiating objective must be to include in GATT a social clause that addresses unfair trade advantages gained through repressive working conditions. Competitive advantage in trade should not be derived from the denial of the right to freedom of association, the refusal to insure a safe work environment, the exploitation of child labor, or other unacceptable practices.
- The impact of the various codes agreed to in the 1979 Multilateral Trade Negotiations (MTN) needs to be assessed and greater attention should be placed on enforcing these agreements and redressing inequities that have appeared. The Government Procurement Code should be renegotiated to provide true reciprocal market access with existing exemptions retained.
- The inadequacies of GATT safeguard procedures need to be addressed. The United States should concentrate on exposing trade restrictive measures and should develop procedures for negotiating agreements that would bring some order and stability to trade in import sensitive products, as well as products and commodities where worldwide excess capacity exists.
- Solutions to the serious problems faced by U.S. industry in the area of counterfeiting and intellectual property rights, such as computer programs, films and recordings, should be a U.S. objective.
- The disadvantage faced by U.S. producers as a result of current GATT

International Trade and Investment

rules on border tax adjustment should be eliminated by means of appropriate changes to the GATT.

With regard to problems in services, solutions must be found through national action and sectoral negotiations. The current emphasis on all-inclusive negotiations on trade in services is misplaced. The trade problems encountered by U.S. service industries are specific and quite diverse. Negotiations must be based on practical solutions for specific current problems so that the huge diversified service industry will not be lumped together inappropriately in multilateral negotiations. U.S. law and practice establishing standards in the service sector must not be weakened.

Instead of broad negotiations on investment rights, emphasis should be placed on encouraging domestic investment. As with trade in services, regulations concerning investment flows should not necessarily be viewed as barriers. The U.S. must not negotiate away domestic employment for business access to foreign markets.

America needs to explore a more realistic general framework for coordinating world trade relationships in sectors characterized by global overcapacity and widespread import controls. The United States operates as if the trade-regulating measures of other countries do not exist—or as if they were irrelevant in determining whether trade is likely to injure U.S. workers and industries.

The temporary and often ineffective U.S. regulation of imports has not accomplished its purpose; other countries have dealt more effectively with international trade to promote industrial development—and employment. At least when there is widespread import injury, and when trade problems have led the major importing countries to apply import restraint, the United States should negotiate an effective multilateral framework for allowing sectoral trade to take place in a rational manner, at the same time preserving our vital economic industrial base and jobs.

The **Chairman**. Quick question. Under S. 1449, we do not impose restrictions on countries that do not have any unfair trade practices, as we define them. Is that correct?

Mr. **Bieber**. That's correct.

The **Chairman**. And Hong Kong, apparently, has none of those. We can freely ship to them. In effect, they appear to have no restrictive trade practices against anybody in the world. They are one of the few countries that are a genuine free-trade zone in essence. Is that correct?

Mr. **Bieber**. Yes, I believe that's correct.

The **Chairman**. Does that mean, then, that we would not impose any restrictions on imports from Hong Kong?

Mr. **Bieber**. No. I wouldn't say——

The **Chairman**. Then I don't quite understand what you mean.

Mr. **Bieber**. Well, we did not say that this bill was all encompassing. We said we supported this bill. I think, Senator, it's true and everyone knows that we have also supported other bills. I specifically made note to S. 1449 because we believe that approach is one approach that could be most helpful in the dilemma in which we find ourselves. That's not to say that we are not supportive of other trade legislation as well.

The **Chairman**. So even if they have no unfair trade practices, we may still want to restrict what they can send here.

Mr. **Bieber**. We would propose that there would be certain limitations.

The **Chairman**. OK.

Now where you make mention of basic rights of workers, and then you go on "such basic rights to free association, organize and bargain, standards for minimum wages, hours of work, occupational safety and health" et cetera, minimum age, are you suggesting that all of those if they do not exist in full flower in other countries, should be unfair trade practices?

Mr. **Bieber**. I'm suggesting, Senator, that those items certainly should be taken into consideration when we consider unfair trade practices because I think they have an effect upon the question of fair or unfair trade.

As an example, in Korea where the rights of workers are extremely limited, certainly that has an effect upon that product being able to come to our country's market under an unfair trade practice.

The **Chairman**. What I'm trying to figure our, Mr. Bieber, is what things we should unilaterally say other countries must match that we have or we will say they are guilty of unfair trade practices.

Mr. **Bieber**. Senator, what I am saying is we ought to say to countries who are doing business with us, who are trading with us, that they ought to recognize and respect the same rights that our Government says workers have a right to expect—the right to organize, to freely choose to organize, the right to safe working conditions, et cetera, as I have pointed out here.

The **Chairman**. You mean that our standards must be their standards if they want to compete in our market.

Mr. **Bieber**. Well, I'm saying that when you take into consideration unfair trade I think you have to take into consideration the fact that in countries such as this the absence of such laws give that product and that country a distinct advantage, and, therefore, an unfair trade advantage against the products produced here.

The **Chairman**. Should they have to meet our environmental standards?

Mr. **Bieber**. Should they have to meet them in their country?

The **Chairman**. Yes. Because that is costly also in terms of meeting the standards that we set down for industry.

Mr. **Bieber**. Well, their products certainly ought to meet the requirements if they are brought into this country.

The **Chairman**. I mean pollution standards. Air and water and dumping standards. Should their factories have to meet the same standards our factories have to meet, because it's costly to meet them. And if they don't, they can produce the product cheaper.

Mr. **Bieber**. Well, excepting that—I'm not sure I would go that far. I think it's an area in which that country ought to be concerned. But I'm concerned about it as a citizen of the world. After all, what they do in those countries can have some effect, I suppose, on the environment of our own country.

The **Chairman**. I'm trying to think of it from the standpoint of competition. You are thinking of it from the standpoint of a good citizen and whether or not they are going to pollute the water and the air of the earth. But I'm thinking of it from the standpoint of competition and cost, much of some of the things you cite—occupational health and safety.

I sense you would have them meet roughly our OSHA standards.

Mr. **Bieber**. So far as protection for the worker, yes.

The **Chairman**. And they should meet our minimum wage standards?

Mr. **Bieber**. Yes.

The **Chairman**. At a minimum.

Mr. **Bieber**. Well, what I'm saying is that if they don't, then I think that has to be worked into the computation as to whether or not this represents fair or unfair trade practices.

The **Chairman**. And our hours of work standards?

Mr. **Bieber**. Yes, sir.

The **Chairman**. Thank you.

Senator Baucus.

Senator **Baucus**. I will end up on the same point, Mr. Bieber. What about, as Senator Packwood suggested, environmental standards, environmental costs? It just seems to me that we are focusing on competition, competitiveness, but that there are other factors in addition to working place costs from an industry point of view. There are environmental costs and there may be other costs as well.

And if we address the labor component, maybe it also makes sense to address other components. And the more we do that, the more we are telling another country what the mix of its costs to its industry should be. What if we had an umbrella cost approach saying if your total costs to your industries are lower or actually the same as ours and you can address the mix anyway you want, would you be interested in that kind of an approach or not?

Mr. **Bieber**. Well, I guess the way I want to answer this is to say that whatever the items are that affect the question of whether or not those products brought into this country we are able to compete fairly against then they should be worked into the equation. If our companies are forced to do certain things, and they are by law, then I think that we should take that into consideration.

However, the point that I made relative to workers' rights and so on, I think that we recognized for instance many, many years ago in this country there was the need to abolish child labor. We have very close to that in some of the countries that we compete against. And many, many other items relative to workers 'safety and so on are thrown asunder.

We think that, first of all, from a moral, humane standpoint, it's proper, but more importantly that our workers and our companies should not be made to compete against workers and companies in other countries who do not practice minimum—at least minimum standards.

Senator BAUCUS. I wonder if you could address a point made by Commissioner Norwood when she was testifying. Essentially, that maybe it's not altogether disadvantageous to our country to have our employment composition move more to the service sector and away from manufacturing sector. Her basic point being employment leaving manufacturing sector does not—is not disadvantageous to this country so long as the output of various industries in the manufacturing sector is growing or increasing. Would you respond to her point, please?

Mr. BIEBER. Well, I guess I would answer it this way: Since 1979, we have lost 1.7 million good paying jobs from this country. I don't think that anyone can argue successfully that we cannot continue to have the standard of living or relatively the standard of living that we have become accustomed to and which I think we are entitled to in this country if we continuously drain off the good paying industrial jobs and replace them with lower paying jobs. And that's exactly what has happened.

In my own union, today we have 50 percent of the employees that we had in 1980 in the agricultural implement section of our union. Not automotive, agricultural implement and heavy industry. It has gone down from 65,000 to a little over 30,000.

We still have upward of 200,000 less workers in auto today than we had in 1978. We are even losing jobs in aerospace. The new technology is going abroad.

Now, if someone can tell me who are going to be the customers of the future, if we have no concern about the loss of these jobs, then I would be glad to listen to that. I don't see that possibility. Unless we can do something to protect the industrial base of this country, we are not going to have the living standard and the type of economy that we've had.

Senator BAUCUS. So it's your point that even though output in our industry in our country may be increasing, if we are still losing jobs, that the standard of living in this country is declining because incomes are declining; namely, the replacement jobs are, if there are replacement jobs, are lower paying jobs.

Mr. BIEBER. Well, they are lower paying, but I also have another problem. Just a few years ago, 2 and 3 years ago, what everyone was telling me was don't worry about the auto jobs that are being lost because we have some new industries, high tech, the computer chip industry, that will take the place of these jobs. No one talked about the rate of pay, which is considerably less.

But I would point out two things. No. 1, the auto industry is a big consumer of high technology, becoming a larger consumer every year. And if you don't believe me, just look at all the new gadgets that are on those cars. But more importantly, I am now concerned about the accuracy of those statements when several years ago I see companies such as Atari move jobs from the west coast to the orient. These aren't high-paying jobs. They are $6, $6.50 jobs. They are going off across the Pacific in search of $1 and $2 an hour jobs.

Now we have done a great deal in our union to encourage retraining. We have spent a lot of money. We negotiated a lot of money with the companies to do this. The problem that we have is what do you retrain people for. What jobs are available. And I can tell you that when you look at what is happening to us, the jobs just aren't there.

And when we talk about high-paying jobs in high technology, you have to understand that the jobs that become available there, and certainly in the Northeast there are a lot of high technology jobs, they are low-paying jobs.

Senator BAUCUS. Isn't it also true that we are losing the technological base. More than manufacturing jobs go overseas. The more we are putting our country in peril because we are losing the technological base and we are losing the ability to progress in R&D and other developing technologies.

Mr. BIEBER. You are absolutely right. We saw this in auto. We saw it in appliance 10 years ago. We are seeing it in aerospace now.

Senator BAUCUS. Thank you.

The CHAIRMAN. Senator Long.

Senator LONG. The one thing that I have noticed is that the Japanese and the Koreans seem to be able when trained at their jobs to do just as good a job of operating these expensive new machines as Americans do. Now I'm not downgrading the American workers, but I have gone through some of these production lines even in Red China and people I see working on those assembly lines who, if you didn't know you were in a foreign country, seem to sit there or stand there, as the case may be, and do a good job at it.

Once we export our technology, take our machines and show them how to do it—and, incidentally, most of the machines I saw in China are being bought from Japan; not the United States—but once they see how it can be done—is there any reason that they can't even make those robots and operate them just as well as we can?

Mr. BIEBER. Well, no, Senator. I might just say this. I, too, was in China within the last 6 months. And, of course, it depends on what assembly line you look at. If you look at an automotive assembly line, they have got a long way to go to catch up. That doesn't mean that they can't. Some of the other assembly lines, as you point out, are very true—making gears and so on.

And if you go to Japan, you also see many names of equipment that were very well known here. Today, of course, they are doing a great job of taking away our jobs in the tool industry, exporting their machines here.

The truth of the matter is if you go to Japan, you don't see an automobile built any differently than you do in the United States. As we have redesigned the car, brought on the new plants and we have got some that have been built totally from the ground up; other plants that have been revamped—we have state-of-the-art plants here. There is no question about it. And we can and I would submit that we do compete from a productivity standpoint.

If you look at the auto industry from 1981 through 1984, productivity has increased by 35 percent. That's a pretty healthy increase. It's not that we can't compete with them, but we have to be able to compete on a level playing field.

The over-valued dollar has made it extremely difficult. In Peoria, IL, I mentioned Agricultural Implements (AgImp) and heavy equipment. Peoria, IL, we produce heavy equipment there. A piece of equipment that comes out of that plant retails for about $265,000. If you look at where the dollar to the yen has been, it means that Kamatsu, who is the chief competitor, everything else being equal, Kamatsu's product can go to the market $65,000 less than the product that we produce in Peoria, IL.

And I would submit to anyone you cannot overcome that by productivity and you can't overcome it by reducing wages, unless you want to put everyone in a soup line.

So that's some of the things that we've had to face. Another part of my argument is that the American companies have now decided, and for various reasons—Chrysler took the position when the voluntary restraint agreement was lifted, they decided not to produce their new P car, which was a small car entry in this market. In place of that, they have worked out a joint venture with Mitsubishi. That will come to this country, and we will have about 50 percent of the content in that car we would have had in the P car. That's also true with the joint venture in Freemont, between Toyota and General Motors. It will be true with the Mazda plant that is opening near Detroit. It's true with Honda and Nissan who are producing here.

And part of my argument is that our own companies have now made a decision to go offshore with the small car and not to invest and develop and to build it here. Now that's with the exception of the Saturn plant that is to be built in Tennessee, and I won't go into that because I think everyone has read enough about that as I have in the last 5 or 6 months to be somewhat familiar with what that venture is.

We would also hope to be able to work out similar agreements with Ford on their small car, Alpha, and Chrysler with their Liberty project. But we have concern about these small cars that are being lost to overseas production.

If you look at 1988 predictions, that's a fair piece of the market.

Senator LONG. Thank you.

The CHAIRMAN. Senator Mitchell.

Senator MITCHELL. Thank you very much, Mr. Chairman.

Mr. Bieber, I think you've put your finger on one problem that is very difficult to deal with, and I would like to ask you about it. You make reference in your testimony to prior Japanese import and investment restrictions in the auto industry. Those practices no longer exist, but the past practices do have a current impact on the U.S. auto industry.

My question is: Should our unfair trade laws permit U.S. industries to seek relief from unfair trade practices that have been terminated? The practices themselves no longer exist, but they have created an unfair market advantage that does continue to exist.

Mr. **Bieber**. Then I think the answer is yes because it's all part of the problem in the equation.

Senator **Mitchell**. In your statement you refer to on page 2 unfair trade practices in Brazil and Mexico. Are you able to provide us now any more detail on those types of practices?

Mr. **Bieber**. Well, it's basically the same thing that I previously covered in that—I thought I tried to cover in my answer to the chairman. You have wage structures, obviously, that are far less than ours. You are talking in terms of $2-an-hour jobs. In addition to that, you have countries where the right of the worker to freely organize is inhibited. Safety standards are far below what our minimum requirements are here; and the whole thing that I raised before. All of that does go into this whole equation and does have an effect upon our industry's ability to compete.

Senator **Mitchell**. So you would regard those as unfair trade practices; not as natural competitive advantages that a nation might have.

Mr. **Bieber**. I think that unfair trade practices—unfortunately, I have to say this. I am also concerned about the fact that our own domestic suppliers take advantage of those situations and import those products from those countries, both finished product and basic parts. And this is becoming more and more of an increasing problem.

As I said, we will have additional pressures coming from Korea very shortly, and I might add from Yugoslavia as well. They do produce a car there. As a matter of fact, they have dealerships in this country now. I saw a couple that sprung up in Detroit within the last couple of months. I've seen the car from a distance. It's less than $4,000. It's a small vehicle, but it obviously will have great pressures against our small car production here.

Senator **Mitchell**. Do you agree that current U.S. trade laws are inadequate to respond to the practices of other nations which adversely affect U.S. commerce?

Mr. **Bieber**. Yes; I think I have said this many times. The problem is that I think we are playing under a set of rules that no one else is. We have, you know—we contend that our policy is a free market policy. I don't know when that existed. It certainly hasn't been around in recent years.

Every other country does things to protect basic industries, such as auto. And at the same time, we allow our market to be inundated with imports. And, quite frankly, we are paying a terrible price for it.

By 1988, if you look at the import, that are projected, if you look at the transplant plants that are projected, and I think they are both absolutely correct, the number of cars that we will be producing in this country, pure domestic cars, will be very close to the number that we produced at the height of the recession in 1982. And in my own union, we had 300,000 members laid off at that time. That didn't take into consideration a number of those in related industries.

Senator MITCHELL. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Danforth.

Senator DANFORTH. Mr. Bieber, back in 1981 when we went through the problem at that time of the auto industry, a number of us introduced quota legislation and voluntary restraints were entered into. The thought that I had at that time, in fact, that I expressed publicly, was that we could provide and should provide short-term relief to the auto industry because it was on the skids. At that time, Chrysler's survival was threatened, Ford's survival was threatened and we thought we were going to lose it.

But the position I took at this time was that this is just temporary relief. That 2 years, perhaps 3 years, of relief would do it. That the Government couldn't keep the auto industry alive forever. And that while we could provide some short-term help, the future of the U.S. auto industry depended on the auto companies and the auto workers being able to produce a competitive product and to sell it at a competitive price.

Well, the 2-year voluntary restraint was extended to a 3-year voluntary restraint, was extended to a 4-year voluntary restraint. I joined the fray when it was lifted saying, well, we shouldn't lift anything without getting something in return, which we didn't.

But I still felt that you just can't keep administering artificial respiration forever. Eventually, the patient has to breathe for itself.

I think what I hear you saying today is that things are not only not getting better, they are getting worse. There is going to be a new inundation of cars from Korea. I believe that the Pony had 11 percent of the import market of Canada its first year. Pretty good test market for the U.S., I would think, Canada.

Yugoslavia is going to be producing cars. And I think what you are saying today, although not quite in so many words, is that the U.S. auto industry is not able and will not be able to keep up with world competition unless the government provides it with some kind of protection.

Mr. BIEBER. I don't know if I want to use the word protection, although I'm not as hesitant as some people are to talk in terms of protection of American jobs, American standard of living. I think that is a part for Government to play.

Let me go back, if I might, just for a moment, Senator. You are right in that many of the statements made back in the 1980's—and I say to you that I'm very thankful that at that time you took the lead in bringing about the voluntary restraint agreement because without it I don't think I would have had an opportunity to sit down at the table with Chrysler—and not just that—but some other things with Chrysler just a few weeks ago. We were losing that company.

Ford was fast going under. VRA certainly helped, but the employees and everyone else made sacrifices and contributions to that as well.

A couple of things happened along the way, though, that we didn't get quite the help that originally I think the voluntary restraint agreement indicated we would get. As you well know, we ran headlong into a deep recession. And, unfortunately, the number of cars, the percentage of the number that came into our country was far higher thao people expected when we looked at the original figures of VRA.

In addition to that, I think a lot of people probably underestimated the amount of time that it really takes to develop a car, to change an industry around. And, you know, we've made tremendous strides in that.

Senator **Danforth**. Do you think we've done it?

Mr. **Bieber**. Well, I think we have to a great degree. Not totally. There are still many things that can be done. We continue——

Senator **Danforth**. Let me just ask you because I only have a few minutes. Do you think we have made good use—we being the industry and the UAW—have made good use of the voluntary restraints of 1981 to 1985? And do you see any end in sight for the need for protection for the auto industry?

Mr. **Bieber**. I think we made strides. I think that if you look at the agreements that we negotiated, they are there for everyone to see. We have done a great deal in worker involvement. We've done a great deal in reducing costs in many areas.

The thing that I'm concerned about is that the auto companies, themselves, for one, have made a decision to some degree write off the small-car industry. We are attempting desperately to try to head that off. But, of course, as I said, the recession hurt us. The over-valued dollar, obviously, hurt us.

And when you talk about the welfare of the industry, I think we have to also recognize that many times when we see some of those profit figures that may go to the welfare of the industry, but it doesn't necessarily mean that the needs of the workers and the communities in which they live have faired as well because they have not.

It seems to me that we have to take all of that into consideration when we think in terms of some orderly procedure to see to it that a very important industry in our country is preserved for the future. It's important to our economy, but I think we also have to look beyond that. It's an important industry to the defense of this country as well.

And I'm concerned as I travel across this country and I see it in every single city I go into, large and small, more and more and more plants that are vacant. And that troubles me a great deal.

Senator **Danforth**. Thank you, Mr. Chairman.

The **Chairman**. Senator Chafee.

Senator **Chafee**. Thank you, Mr. Chairman.

Mr. Bieber, it seems to me that the problems of the automobile industry in the late 1970's and early 1980's derived, at least as I saw it, from a host of problems. One of them was sloppy quality, poor design, and poor mileage. And I think both the management and workers have tackled that. It's my judgment that now you are producing a product that qualitywise is probably competitive.

But you have made a conscious decision—you, the workers—that you are not going to be competitive wagewise. And, indeed, you just conducted a successful strike against Chrysler, and you have emerged with the highest industrial wages in the Nation. I suppose the automobile wages now, with fringes, are something like $24 an hour, close thereto, at least in the studies I've seen.

Now that's fine. But what you have are wages with fringes that are far higher than most industries in the Nation. And as a result, you are having difficulty finding a market for your product. The domestic market for automobiles is there clearly because the foreign automobiles, as you mentioned, are flooding in. Let's just stick to Japan because I don't think we can say that they are suffering under the difficulties that you mentioned exist in some countries—that is labor working under very extraordinarily difficult situations.

Now if those involved in the industry, namely the workers, aren't prepared to be competitive in wages and, indeed, go out and strike, and a successful strike, when they are already over $20 an hour and come up to $24, $25 an hour, what can you expect us to do here? Are we meant to respond—am I meant to say to my people in Rhode Island who are getting $7 or $8 an hour with fringes that they can't buy the Pony or the Yugo or whatever it is in order to protect the jobs of those in Detroit making $24 an hour with fringes? What's the answer to that?

Mr. BIEBER. Well, first of all, Senator, I think we have to compare apples to apples. And, first of all, it's not a question of an auto worker taking home $24 an hour.

Senator CHAFEE. I didn't say taking home. I said with fringes.

Mr. BIEBER. Well, OK. I just said it's not a question of taking home $24 an hour. It's a question of some who are taking home more like about $11.50 an hour.

But then I think we also have to compare that to the industry that that worker is in. And that's an industry whose productivity has increased 35 percent over the last 4 years. And I think that has to be taken into consideration.

Now let me say this since you raised it about the successful negotiations at Chrysler. I prefer to use those terms. There was a strike that ensued. I think that's recognized as part of the right of workers and their employers to sit down and bargain.

Senator CHAFEE. Nobody challenges that.

Mr. BIEBER. But let us also recognize that in that settlement the vast majority of the items included in that settlement were only to bring the people back to parity and there was some additional upfront money which was recognized by the company was given to the workers to repay somewhat the losses of wages that they had encountered during the difficult years. Now nowhere near what it represented, because you are talking in terms of $1,700, $1,800 compared to $22,000 or $23,000 across the board.

Other than that, the Chrysler agreement does not represent anything over and above the General Motors and Ford agreement. The first 2 years are identical.

Senator CHAFEE. My time is limited, and I don't want to get into a discussion of the agreement one way or the other, but the auto workers overall are the highest paid workers in the Nation, and considerably higher than anybody else with a contract that I think anybody would say is splendid. That's fine, if that's what they want. But they are in a competitive field.

And as a result of these contracts, plus the high dollar, plus factors like complete health insurance. As you well know from your experience in Chrysler the health coverage now costs more than the steel does in an individual automobile, first dollar coverage. That's what they want, and that's what they have got.

To then come here and bemoan the fact that foreign automobiles are taking a bigger and bigger share of the market isn't being completely realistic in my judgment. You can't have it both ways. If you want these extraordinarily fine benefits, higher than any other worker in the country is getting, all right. But just remember that the result of that is going to be a reduced share of the market.

I regret that what you predict here is probably going to be true in 1988. To put it bluntly, I think you have priced yourself out of the market or are in the process of doing so.

Mr. BIEBER. Well, Senator, I don't want to be argumentative, but, again, I make the point that the auto worker whose wages you allude to also works in an industry with the highest productivity in the world. Now when you compare it to the $6 or $7 an hour jobs in your section of the country, the problem is that we are being—we are being forced to compete against wage rates of $1 or $2 an hour in the foreign countries, with all the other things I mentioned this morning.

Senator CHAFEE. I don't think that applies to Japan, Mr. Bieber.

Mr. BIEBER. Pardon?

Senator CHAFEE. I don't think that argument would apply to Japan.

Mr. BIEBER. Well, some of it does. Not nearly to the degree that it does in Korea and so on. And the problem that we have is that if what we are saying is we just have to chase the lowest common denominator, then I don't know where that ends. Now it's shifting from Japan to Korea to Malaysia, and when we are done there, we will go somewhere else.

And I would have to suggest that if what we are saying is the American standard of living now has to be tied to the lowest wage rate that we can find in the world, and we have to bring our wages down to compete against them, that America is in deep trouble.

Senator CHAFEE. Well, my time is up. But I'm not suggesting that. I'm suggesting there is a difference between the absolute peak—$24 an hour with fringes—and what the average, for instance, industrial wage in the United States, which I suppose is around $12 or $14 with fringes. My time is up.

The CHAIRMAN. Senator Symms.

Senator SYMMS. No question, Mr. Chairman.

The CHAIRMAN. Let me pursue what Senator Chafee is talking about, I think.

He's not suggesting that you compete with the Korean wage earner. I think what he is asking is why should the autoworkers get so much more money—what's the principal industry in your State?

Senator CHAFEE. Well, the textile industries, the copper wire industries.

The CHAIRMAN. All right. Why should they get so much more than that? Or why should they get so much more than the lumber worker in my State?

My hunch is the average age, the average education, the average physical and mental difficulty of the task in the two industries is roughly similar between lumber and auto. Why should the autoworker get so much more money that it makes domestic cars uncompetitive, and, therefore, my lumber worker who makes $5 to $6 to $7 less cannot afford to buy the American car and won't be allowed to buy the foreign cars?

Mr. **Bieber**. Well, Senator, first of all, I would like to reduce that figure as well, but I'm forced to go to the collective bargaining table, negotiate for health care benefits, which in Japan—and Senator Chafee mentions Japan, which in Japan is provided for under national health. I happen to think that we ought to have a national health program here as well, and we ought to take that off the back of that employer in this union, and we can reduce that wage rate that you talk about considerably.

On the other hand, I have to keep repeating that the autoworkers while they earn good wages also work in an industry that has high productivity. Now are we saying that every worker in America should receive the same wage regardless of the productivity factor?

Productivity has increased by 35 percent in the auto companies in 1981 through 1984. There is no other industry that I know of in this country that comes anywhere near that. So I think that has to be taken into consideration when you measure that off against the wage rate.

And to repeat, there are many things that we have to talk about, negotiate, at that table that in the competitor countries you don't because they are provided. And health insurance is a big item.

And I might just say—Senator Chafee mentioned this before—in Chrysler we have worked very hard and successfully to reduce the cost of insurance benefits, insurance costs. We have done a lot of things. We've been very innovative in putting new programs into place where we have been able to successfully cut down what I think was unnecessary costs. But I submit, you know, that the provider has to play a role in that. I don't know when I go to the doctor and take a child or a grandchild and he says you have to have 22 tests, who am I to argue it's only 10.

Now we have begun to do some things together to attack those situations which do have a result in reducing some of the costs.

The **Chairman**. Do you really think that the U.S. Government is better at monitoring health care costs than the UAW and the auto companies?

Mr. **Bieber**. Well, Senator, I just said we have been doing some pretty important things there, but if I just look across out of my office window, I can see a neighboring country. On a clear day, I can see Windsor, Canada from my office window. And if I look at the benefits and the costs of the national health care program that's been provided and the costs over the last 10-year period, then I have to say the cost has been significantly less there than it has been in the way that we are trying to do it.

I'm not trying to get into the national health care argument here this morning because we obviously don't have enough time to cover all that. All I'm saying is you have to match apples to apples. And when the good Senator Chafee says, you know, it's $23 or $24 including fringes, that's correct. But we have to cover hospital costs. We have to cover pension costs, et cetera, et cetera, which isn't done the same in every other country.

The **CHAIRMAN**. Senator Long.

Senator **LONG**. No further questions.

The **CHAIRMAN**. Senator Bentsen.

Senator **BENTSEN**. Thank you very much, Mr. Chairman.

I was just looking at some figures that were given to me by Dr. Norwood who had testified earlier about what has happened to real hourly compensation in the U.S. manufacturing, and that it's lagging far behind the wage growth in Japan, United Kingdom, France, and Germany since 1980. Then I was looking at Dr. Thurow's article in the Economist recently; it says: "Relative to the price of capital, American wages were 37 percent lower in 1983 than they were in 1972." In Europe, he says: "The wages have risen relative to the price of capital until very recently."

I'm not speaking about the automobile industry because I don't have the numbers on that. But I'm saying that is what has happened across the spectrum of wages in manufacturing in this country.

I was very pleased to see your support of S. 1449. And I was interested in some of the reaction we had in the introduction of that piece of legislation. When I turn around and look at what is happening today—I read in this week's Journal of Commerce that representatives of the European Community, Common Market, have been in Tokyo this week trying to set targets on how much the European Common Market will accept in the way of Japanese trade surpluses. It seems to be all right for them to take that kind of an approach. But there's a great deal of concern for us concerning this country.

Now let me ask you: This concerns the Koreans and what they are doing in the way of competitiveness and wage scale. Some of the staff of this committee was in South Korea this summer. And they were told that this new automobile of the South Koreans, small, compact, was going to be selling for far less than the cost of the Japanese comparable car. How many of those cars are being sold in Japan?

Mr. **BIEBER**. How many are being sold——

Senator **BENTSEN**. South Korean cars. Japanese buying the Korean cars. Are the Japanese buying an awful lot of those now since——

Mr. **BIEBER**. I don't have the exact figure, but they will probably sell about as many as they do American cars in Japan because I expect they will probably have as much of a problem getting into that market as ours do.

Senator **BENTSEN**. There is not that big a cultural difference, is there?

Mr. **BIEBER**. No.

Senator **BENTSEN**. There is not that great a difference in the automobile, quality or its size, is there, between the Japanese car and the South Korean car?

Mr. **BIEBER**. Well——

Senator **Bentsen**. You get the feeling, then, that there is some kind of limitations or barriers on South Korean cars even if they are sold for much less coming into Japan.

Mr. **Bieber**. I'm not sure, Senator, and I don't want to—my offhand assumption is that they will probably not fare a great deal better than the American product. And there are a couple of reasons for that. We all know what the American product faces when it goes into Japan.

In addition to that, I have to say this: That I admire the Japanese in that they do show loyalty to their own product. And sometimes that's not exhibited to the extent that I think it ought to be here in America where we do quite the opposite.

So far as the quality of the car, Senator, I think you have to look at—there are actually two different cars. No. 1, the Daewoo Co. will produce a car for General Motors. It will be sold as a General Motors car in this country just as the Sprint and the other cars are sold as General Motors cars here that are produced by Isuzu of Japan. Hyundai is exporting their own car; have been exporting it to Canada, and will bring it in here. I've heard different degrees of the quality of that car. I really don't know.

I would dare bet that the car that is imported from Daewoo under a General Motors nameplate will be a high-quality car. There has been a great deal of investment made by General Motors in the development of that car.

And, of course, now you have the agreement that is being worked out with Chrysler with Samsung and Ford with another Korean company that will bring in parts. And I will be surprised that eventually they won't bring in completed cars as well.

Senator **Bentsen**. It seems to me that as we downsize and we out-source we lose part of the constituency fighting for the manufacturing base in this country.

Mr. **Bieber**. Well, there is a great deal of imports—parts that are now being imported from Korea, from Malaysia, and I do not expect that we are going to see that figure become lower. It's going to increase. As I just said, Samsung is a company that Chrysler Corp. has just recently worked out an agreement with for the importation of parts.

General Motors decided to import roughly 80,000 cars from Daewoo. There is upward of 300,000 cars that are being imported under the Chevrolet nameplate from Isuzu and Suzuki.

Senator **Bentsen**. Well, the point I'm making, though, is that as that happens, you have fewer and fewer of those people that fight to keep a manufacturing base in this country, as international companies find it to their benefit to out-source to bring components from other countries.

Mr. **Bieber**. Yes.

Senator **Bentsen**. Thank you.

The **Chairman**. Are there other questions?

Senator Baucus.

Senator **Baucus**. Very briefly, Mr. Chairman.

Senator Mitchell asked about whether prior unfair practices—certainly, that is Japanese targeting, protectionism—should be treated as an unfair practice today. Your response was yes it would because of the adverse effects that it has. And I agree that that's something that we should address.

It's my understanding that, as you pointed out, the problem is getting worse in that not only Japan and Korea and others, but that other South American countries are now starting to try to follow and put in place the Japanese practices, the kind of mercantilistic practices that have worked in Japan. Brazil and other countries are starting to subsidize the financing of domestic industries and to try to do even more than they have thus far. And this leads to the problem of rising unfair trade practices around the world. They are getting worse; not better. And the deterioration of the GATT which isn't addressing these and so forth.

My question really comes down to this: The degree to which you have thought about which practices should be classified as fair and which are unfair. That is, what is fair and unfair to me is a little bit like Senate rules around here as to what is germane and what is nongermane. I mean it's germane if you are for it, and it is nongermane if you are against it. I think the same applies to unfair trade practices. I mean if they do it, it's unfair. If we do it, it's fair.

So what practices should be generally treated as unfair and fair. You think that foreign lower wage rates and poor working place conditions should be classified as unfair. That is certainly something we don't want to do.

On the other hand, some of the targeting practices and some of the subsidies and so forth, which other countries engage in more than we, could be classified as unfair. That is, they have got to stop it. Or that could be classified fair because we should start doing it.

My question is: Can you kind of give some guiding principle as to what should be unfair that all countries should stop? And what should be fair and we should be doing more of because it is working?

Mr. BIEBER. Well, I gave some thought to that because I think that's really one of the questions, one of the three questions that was attached to the release that said everyone should address themselves at least to one of those three questions.

And that one of those questions was: How should fair and unfair trade be distinguished? And I guess that's exactly what you are saying.

Senator BAUCUS. Right.

Mr. BIEBER. Well, I think for the purpose of U.S. action the distinction between fair and unfair trade is really less important than the impact of trade on the domestic industry and the policies that we need to have to effectively deal with it.

As I said before, I think we must take action to make abuses of labor rights an unfair trade practice under our law and under international agreements. This would certainly increase the chances of eliminating these abuses. And beyond that, I'm not sure that I'm any more qualified to give you a direct set of rules as to what falls into fair and unfair practices.

I would suggest, Senator, that we have an extremely critical situation facing us. An industry that unless something is done to give us a fair shot, we are going to see it decline substantially. And it isn't going to be long range.

Senator **Baucus**. So you wouldn't worry too much about the question. That is, you are less concerned about what is fair and unfair. You are more concerned about——

Mr. **Bieber**. I'm more concerned about the results.

Senator **Baucus** [continuing]. What the results are.

Mr. **Bieber**. Finding a resolution to the problem.

Senator **Baucus**. That is, to set a level that our trade with a certain country can only be a certain percent of GNP or something. Let them worry about it. But it is no higher.

Mr. **Bieber**. I know this, Senator. That what we have been trying to do and what we have done—and I think many people have been well-intentioned—hasn't worked all that well. And I'm afraid many people see the auto sales figures of the last couple of months and they say, well, everything is just rosy out there. It isn't.

And I would suggest to you that the sales figures of the first 10 days of November certainly do alarm me. I have concern as to whether or not that isn't going to be the norm rather than the exception.

The figures that I put together in the statement that we gave to you are solid figures; 1988 is not very far away, and unless we do something and do it quickly, we are going to see this industry literally torn apart. And what we will have left of it will produce very few jobs, good paying jobs, for American workers.

Senator **Baucus**. Thank you.

The **Chairman**. Senator Chafee.

Senator **Chafee**. Thank you, Mr. Chairman.

First of all, I want to say that I read part of the AFL-CIO statement here at the back of your testimony, Mr. Bieber, and I certainly agree with some of the points the AT&T divestiture imports of telecommunication products have inundated the market.

What I believe in is access to other markets, and enforcement of some laws that are being violated. In that statement it is mentioned that the copyright law must be extended. I couldn't agree with you more on that.

Let me say as far as the productivity of the auto industry, the increase—I think you mentioned 34 percent since 1980. That's great. Am I correct in that?

Mr. **Bieber**. Eighty-one, 1984.

Senator **Chafee**. Eighty-one. That's wonderful. And I hope the effort can continue.

I'm familiar with what you have done in Chrysler in connection with trying to police the health costs because I've heard your fellow director, Mr. Califano, speak eloquently on this subject several times.

You get right back, though. You do have first-dollar coverage, and I think anybody who has studied this knows that first-dollar coverage leads to excesses.

I also regretfully conclude that your predictions for 1988 are probably right. You are much closer to it than I am. And unless those involved—that is, management and labor—are prepared to price their product and reduce their costs commensurate with the imports—you will not be able to compete with imports. No one is suggesting that the autoworkers become abject slaves, but I think when you are in a $24-plus an hour including fringes, you are pricing yourself out of the market. And I wouldn't suspect that you are going to find this Congress very sympathetic to doing something for you when you are at those levels and you are competing mostly with the Japanese who I don't think we can claim fall into any of the criticisms that you might have for Korea or even Yugoslavia.

So I just would hope that all sides would exercise restraint in future negotiations or you will be quibbling over a smaller and smaller piece of the pie.

Mr. **Bieber**. Well, Senator, I might just say this. I think the record shows we have done exactly that. If you go to 1982, 1984 negotiations, the recent Chrysler settlement—I point out again the 1984 settlement, every economist in the country said this is not an inflationary settlement.

Let me also suggest to you, sir, that if the answer to our problem is merely to start round after round of reduction in wages, then somebody has to tell me where that ends because if you reduce the wages $5 an hour here, then don't we have to assume that the Japanese will do likewise, the Koreans will do likewise.

Senator **Chafee**. Well, that didn't occur when you went through that competitive thing.

Mr. Bieber, all I can say is—and I guess you are used to working in this stratospheric area of $20, $23, $24 an hour. That isn't the norm for the United States of America. And it isn't that anybody is asking Chrysler or Caterpillar or any other workers to get down to $2 an hour 'But you are just up there in the top, and it affects the price of your product.

Mr. **Bieber**. But, Senator, I have to keep reminding you that it is also an industry that has had phenomenal figures in productivity. And if you say to me that an industry with a 35-percent increase in productivity to pay two bits an hour increase as opposed to an industry that has had a 3-percent increase of productivity paying a nickel, I suggest to you that you have to measure apples to apples.

Now I'm not suggesting that the autoworkers' wages aren't good, that their benefits aren't good. I'll repeat again some of these benefits we shouldn't have to negotiate at a collective-bargaining table, but we do. But by the same token, I'm going to keep defending the fact that those autoworkers have produced productivitywise to earn those wages.

And I might say this, Senator, on the health care benefits. It goes beyond Chrysler. We did that before we moved to negotiations, but in Ford and General Motors in 1984, we made substantial changes there to reduce those costs as well.

Now I might say that I could make the same argument for people sitting on the other side of the table, and the remuneration that they have received.

Senator **Chafee**. My remarks weren't restricted to labor. They cover management as well. I think management in the auto industry made some ghastly mistakes in design and mileage and quality. And you can stick with your arguments, Mr. Bieber, that you've had these increases in productivity, that you are making efforts in the area of health care. But when all is said and done, you've got a product that is $1,000 to $2,000 more expensive than the competition. And not a better product, apparently, judging by the way the American people make their choices.

On that basis, unless something is done—and I certainly wouldn't be in favor of restricting imports unless something is done by management and labor—the dire predictions you made for 1988, I suspect, are going to come true.

Mr. **Bieber**. Senator, if I might just point this out. An automobile coming from Japan, a $6,000 automobile, everything else being equal, the differential that we've had between the dollar and the yen, there is a $1,500 landed-price advantage for that car. Add to it the manipulation of the tax that they run back to the domestic market as opposed to their import, and you have got $1,900 to $2,100.

Now I'm not saying that everything else is equal, but I'm only pointing out that in that area alone you are talking $1,500 to $2,100 on a basic $6,000 automobile. You know, the auto worker can't compete against that by productivity, and you can't compete against it by wages either.

I understand what you are saying. I have made my points to point out that it's not a case of just getting additional wages, et cetera, without producing within that industry. But I would submit to you that we can't handle this situation just by reducing wages.

If we do that, then common sense tells us everybody moves to the area where the lowest wage is paid. Unfortunately, our own domestic companies are doing too much of that now.

The **Chairman**. Any other questions?

Senator Bradley.

Senator **Bradley**. Mr. Chairman, let me just say in following up that exchange that the original problem here flowed from domestic American economic decisions being taken without any thought about their international repercussions. In 1981, 1982, the United States decided to finance a big budget deficit with high interest rates. And that decision was taken as if it were free, no problem.

The result was a Third World debt problem that caused capital to flow into this country like a gusher from Latin America and elsewhere, and also caused U.S. banks to stop lending money abroad. U.S. bank lending went from $120 billion in 1982 to $20 billion in 1984. That resulted in a dollar that is not competitive. And when that happened—and I tend to agree with Mr. Bieber—it is pretty tough to make up for a 25-percent subsidy or a 30-percent subsidy to foreign imports by telling workers to take wage cuts. And particularly to ask for wage cuts without ever ensuring that the company is going to make the right kind of investments in plant and equipment.

So I think that we have to see this problem in its total context and not simply say, well, the problem is wages, here. I think the problem is economic policy that is made without any sense of its international repercussions.

I tend to agree with Senator Chafee that we don't want the response to be as bad as the original cost, but I also think it's incorrect to say that the problem is merely the wages of UAW personnel. I just can't buy that.

So let me, with that preamble, ask a basic question about whether the value of the dollar is too high. I should say it's overpriced, because that's what it is. It's overpriced. It's not competitive.

Would you support a policy of intervention in the exchange market to get the value of the dollar down?

Mr. **Bieber**. Yes, sir.

Senator **Bradley**. Let me ask you as well: Given what the nature of the changing economy is going to be in the next 5 to 10 years, there has got to be adjustment. And there has got to be trade adjustment assistance. It is keyed to getting workers new skills and new knowledge so that they can have an opportunity to stay employed. Do you agree with that, Mr. Bieber?

Mr. **Bieber**. Yes, Senator. And if I might just say—and I don't want to belabor the point—but you understand that in 1982 and 1984 because of a lack of Federal funds for training, we went to the collective bargaining table and negotiated a cost of $0.15 an hour in General Motors and Ford and that same $0.15 is carried over to the agreement I just negotiated with Chrysler because we wanted to be able to do two things. No. 1, retrain people who will be reutilized in the auto industry. We've gone through a drastic change in design and product line and plant equipment and plant facilities. And we need to retrain those people who are being displaced by that new technology to take the jobs that that new technology provides. Heretofore that didn't happen.

In addition to that, we are training people who are no longer going to have a future in the auto industry for jobs in other areas. Unfortunately, one of the problems we have is a lack of jobs. But that is an additional $0.15 that goes into that wage equation that we have had to negotiate to retrain our own people. And I think that's a little bit unfair. I think the Federal Government ought to accept that responsibility and relieve us of that cost.

Senator **Bradley**. Well, let me say, Mr. Bieber, this committee agrees with you on that point, and we hope that by the year's end we will have a trade adjustment bill that has passed the Congress and signed by the President. We need to do that, and I think the committee is in agreement.

Thank you for your excellent testimony.

Mr. **Bieber**. Thank you.

The **Chairman**. Mr. Bieber, thank you very much.

Mr. **Bieber**. Thank you very much, Senator.

The **Chairman**. Let's move on to Herman Starobin, Robert Eisen, James Mack.

Let me say to the other panels that are coming on, we are in a bind and we may have to reschedule on another day of hearings some of the people who are scheduled to testify. I don't know how far we are going to get. I have to meet at 1 o'clock with some House members on the debt reduction panel, and I've got to leave here at about 12:30, a debt reduction conference on Gramm-Rudman, in order to do some preparation for it. And I'm not sure who can stay to preside. I don't know if Senator Bradley can or not. We are in a bind, and we will go as far as we can and see what happens.

Senator **Bradley**. This is a rare opportunity, Mr. Chairman.

The **Chairman**. I understand that. I'm reluctant to leave you. [Laughter.]

Senator **Bradley**. Just so you leave without a quorum, right? [Laughter.]

The CHAIRMAN. Mr. Starobin, go right ahead.

STATEMENT OF HERMAN STAROBIN, DIRECTOR OF RESEARCH, INTERNATIONAL LADIES GARMENT WORKERS UNION, NEW YORK, NY

Mr. STAROBIN. Thank you, Mr. Chairman. My name is Herman Starobin. I'm an economist and director of research with the International Ladies Garment Workers Union.

We are pleased to have this opportunity to share with you our views on U.S. trade policy, particularly as it relates to imports of apparel from the low-wage areas of the globe. I'm going to cut back on my oral presentation, and I hope that the complete text of my statement is included in the record.

The key factor fueling the flood of apparel imports into the United States is the low-wage level that exists in the major exporting countries. Data compiled by the Bureau of Labor Statistics and the International Trade Commission show that compensation, including whatever fringes may exist in cash or kind, of apparel workers in the top 20 low-wage nations shipping apparel to the United States range from 2 percent of the U.S level in Bangladesh to a high of 25 percent in Singapore. I have appended to my testimony an appendix which details the wage levels of 20 major low-wage exporting countries.

These data are for factory workers only, and do not include the even lower compensation paid to cottage industry workers in these countries

In a labor-intensive industry such as apparel, where wages account for as much as one-third ot the wholesale cost to produce in the United States, labor cost savings are literally the only reason for the massive growth in imports. The technology in the industry is universal and the styling and sizing is done by and for the American market. There is no unique foreign-made product. There is only the assembly of what would otherwise have been produced in the United States, but at a fraction of its cost.

Mr. Chairman, considerable theoretical and certainly emotional support has been developed for the concept that export-led development would bring heretofore agrarian countries of the Third World into partnership with the industrialized nations. It has also been assumed that apparel production, simple in technology and requiring modest capital investment, could provide the initial steps toward industrialization.

Those who have projected this concept have stressed that export-led, labor-intensive industrial development would lead to the accumulation of capital in the foreign country. This capital, in turn, would be used for investment in economic development, leading to reductions in the typically high levels of unemployment that prevail in these underdeveloped areas. Export-led development has also been counted on in recent years to permit payments of interest and principal on the debt incurred by Third World countries and held by the American and European banks, the World Bank or the International Monetary Fund.

The typical Third-World export-dedicated apparel plant's dominant advantage in security contracts is a lower cost than similar operations in either an industrialized country or, as in many cases, some other developing area. Once a country decides to follow the route of export-led development, it is forced to pursue a program aimed at holding down labor and other costs and offering subsidies and aid.

My views on export-led development stem not merely from reading or from theory, but from personal experience as well. Two weeks ago I returned from a visit to the Far East where I served as an adviser to the U.S. delegation negotiating textile agreements. Among the countries we visited was Bangladesh. My colleagues and I were deeply moved by the abject poverty we found there and would like to help these unfortunate people. Yet, I was also deeply impressed with the price extracted from the country and its workers by foreign firms which have encouraged and established there export-only plants.

It was obvious to us that the Bangladeshis were being ripped off by their customers. In one plant I visited, men's dress shirts were being made for export to the United States, the United Kingdom, and West Germany. The local plant was paid about $27 a dozen or about $2.25 each for the completed shirts. The shirts were preticketed with price tags for use in the importing country's stores. They approximated $16 each after currency conversion—more than seven times the amount paid the Bangladesh factory.

The local manufacturers who are underpaid for their work pass along the largest part of their burden to their workers so as to maximize their own returns. In the Bangladesh plants I visited, wages reportedly varied from 900 to 1,200 taka a month for a 6-day, 10-hour per day schedule. In U.S. terms, this worked out to between $28 and $37 a month or from 10.4 to 14 cents an hour. These abysmal wage levels apply only to experienced workers; trainees received considerably less for the first 3 months of employment.

Senator CHAFEE. Mr. Starobin, I read your testimony here and I can appreciate all of that, the trainees and so forth. What do you advise? What is your conclusion?

Mr. STAROBIN. My conclusion is that the policy that we should follow with respect to helping developing countries should be a combination of two factors, Senator. One is the development of an internal market, and I think that's the primary thing that should be done, rather than an export-directed market which helps a very minute elite to the exclusion of any assistance, real assistance, to the poor people who inhabit these countries.

Senator CHAFEE. All right, fine. We'll have a chance for questions.

Mr. Eisen, Greenwood Mills.

[The written statement of Mr. Starobin follows:]

BEFORE THE COMMITTEE ON FINANCE
U.S. SENATE

STATEMENT OF HERMAN STAROBIN, PH.D.,
DIRECTOR OF RESEARCH
INTERNATIONAL LADIES' GARMENT WORKERS' UNION, AFL-CIO

NOVEMBER 20, 1985

My name is Herman Starobin. I am an economist and the Director of Research of the International Ladies' Garment Workers' Union. The ILGWU has over 230,000 members engaged in the production of women's and children's apparel and accessories. We are pleased to have this opportunity to share with you our views on U.S. trade policy, particularly as it relates to imports of apparel from the low wage areas of the globe.

Our nation is at a critical juncture. Unless there is a fundamental change in policy and direction, the United States may well begin to take on many of the aspects of a Third World nation in the not too far distant future. As our manufacturing base shrinks, we can anticipate a growing trend towards a declining middle class and a society increasingly comprised of a relatively small elite, a mass of low-wage workers and heightened unemployment and underemployment.

Many of these trends stem from misguided U.S. domestic economic and foreign trade policies. Our widespread acceptance of free trade, an understandable humanitarian concern for those less fortunate than ourselves and the positive experience we have had with the export of U.S. goods in our own economic development has colored our thinking. Too many policy makers have accepted without careful examination the premise that export-led economic development is, by definition, beneficial to developing nations. Too little attention has been paid to the economic impact of the other side of the coin -- the devastating effect on U.S. business and employment of the massive growth of manufactured imports in recent years.

Trade-induced disruption of domestic U.S. industry cannot be dealt with merely by using slogans like "free trade" or "fair trade". This is particularly true of the apparel industry. Certainly, there are practices followed by nations that could be defined as unfair. Among them are such obvious items as subsidies, tax advantages or other kinds of assistance which foreign governments give to their export industries. More subtle, but also "unfair" are such insidious practices as discouragement of trade unions and collective bargaining in many of these countries and exemption of export industries from labor laws and regulations.

The wide range of subsidies and assistance extended by many foreign governments to their export industries helps encourage their trade. Elimination of such practices would, however, not dramatically alter the economic disruption in the United States caused by ever-increasing imports.

The key factor fueling the flood of apparel imports into the United States is the low wage level that exists in the major exporting nations. Data compiled by the Bureau of Labor Statistics and the International Trade Commission show that compensation, including whatever fringes may exist in cash or kind, of apparel workers in the top 20 low-wage nations shipping apparel to the United States range from 2 percent of the U.S. level in Bangladesh to a high of 25 percent in Singapore (See Appendix A for details). These data are for factory workers only and do not include the even lower compensation paid to "cottage industry" workers in these countries.

In a labor intensive-industry such as apparel, where wages account for as much as one-third of the wholesale cost to produce in the United States, labor cost savings are literally the only reason for the massive growth in imports. The technology in the industry is universal and the styling and sizing is done by and for the American market. There is no unique foreign-made product. There is only the assembly of what would otherwise have been produced in the United States, but at a fraction of the U.S. cost.

Because of the nature of the apparel industry, the elimination of "unfair" trade practices would have a minor impact on import levels. Nor would a greater degree of "fair trade" open significant foreign markets to U.S.-made apparel products. Products made in low wage countries would undercut U.S. producers.

This basic reality is so important that it deserves reiteration. The American apparel industry cannot compete with products made abroad at wages that are as low as one fiftieth of our own. Nor can we reduce the already low wages of American garment workers without creating a shameful Third World of our own. The question is not one of of trade practices that are unfair. The question is one of life or death for the American industry and its workers.

Since the apparel import problem took hold in the 1960's, we have witnessed a steady erosion of the U.S. market. Where once only 4 out of every 100 garments worn by the Americans were made abroad, today over 50 percent of U.S. clothing consumption is of foreign origin. Twelve years ago our industry employed one and a quarter million production workers. Today, despite the increase in population, there are barely 900,000 individuals making clothing in the United States. The unemployment rate in our industry this year has averaged over 11 percent, roughly one and a half times the national average.

Official statistics, however, do not tell the full impact of imports on our industry. They do not reveal the number of new job opportunities that have been lost to imports. They do not reveal the impact on workers and their earnings of short seasons, sporadic work, and the depressing of wage levels by employers as they try to meet foreign competition.

If the textbooks on trade or if our own laws were to distinguish between fairness in trade and unfairness, I doubt these formal definitions would offer any solace to the worker who has lost his or her job or to their families.

The devastating effect of imported clothing on the U.S. industry in recent years has been well documented. What has been less closely examined is the impact of garment production on economic and societal developments in the low-wage apparel producing countries of the world.

Considerable theoretical and, certainly, emotional support has been developed for the concept that export-led development could bring heretofore agrarian countries of the Third World into partnership with the industrialized nations. It has also been assumed that apparel production, simple in technology and requiring modest capital investment, could provide the initial steps toward industrialization.

Those who have projected this concept have stressed that export-led labor-intensive industrial development would lead to the accumulation of capital in the foreign country. This capital, in turn, would be used for investment in economic development, leading to reductions in the typically high levels of unemployment that prevail in these underdeveloped areas. Export-led development has also been counted on in recent years to permit payments of interest and principal on the debt incurred by third world countries and held by American and European banks, the World Bank or the International Monetary Fund.

Had export industries in the various countries been patterned after the historical experience of the development of U.S. exports, matters might have been different. In our economy, production for export is fully integrated. Manufacture is accomplished by the same workers, in the same plants and under the same laws as those governing production for domestic markets. Management and capital sourcing are similar in domestic and export-targeted operations. Not so in a vast majority of Third World operations.

The typical Third World export-dedicated apparel plant, for example, performs only one facet of the range of operations involved in the production and sale of apparel -- assembly. The plant's dominant advantage in securing contracts is a lower cost than similar operations in either an industrialized country or, as in so many cases, some other developing area. Once a country decides to follow the route of export-led development it is forced to pursue a program aimed at holding down labor and other costs and offering subsidies and aid.

The most common step taken by the developing country is the establishment of export platforms, i.e., specially demarcated areas for the production of goods intended for export. These zones are often referred to as free trade zones or free production zones. They may be separate industrial parks or simply designations given to individual factories. These are not to be compared with U.S. free trade zones which are simply duty-free areas. The foreign zones are a world unto themselves, with a variety of laws and regulations that set them apart from the rest of the country.

The special rules that apply to export-dedicated operations vary from country to country. Among them will typically be found the following:

a. Duty free entry of capital goods into the trade zone.

b. Duty free entry into the zone of materials to be used in the manufacture of goods destined for export.

c. Full or partial exemption from personal or corporate income or real property taxes for substantial periods of time.

d. Loans at preferential interest rates.

e. Electric power at preferential rates.

f. Exemption from any existing exchange controls, permitting the free transfer of profits out of the country.

g. Provision of buildings as well as such public works as roads, water supply, etc.

h. Exemptions from labor laws to discourage union activities, exemptions from whatever wage, hour and social security legislation may exist, as well as from regulations relating to pollution, health and safety so as to to insure the lowest possible cost.

In some instances, the entire country effectively functions as a free production zone as, for example, Hong Kong and Singapore.

Turning to export-led development means the isolation of the export zone and its workforce from the national economy and society and the denial to the producing country's economy of a fair share of the profits of the enterprise. The chief beneficiaries of such programs are generally a small number of elite individuals who provide capital to these businesses and, of course, the parent importing firm which enjoys huge profits at home based on the low cost of the foreign assembled product.

Instead of providing funds for further development, the export industry operation of foreign investors often works in reverse. The parent firm usually provides only initial capital which it quickly repatriates. Other capital is borrowed in the foreign country and drained from local development projects. To meet foreign exchange obligations, the developing country is often forced to borrow heavily from such lending institutions as the IMF and private banks.

Export-led development has been touted as a way to reduce the chronic high levels of unemployment in the developing countries. This, too, often turns out to be more myth than reality. The work force utilized by the export platform factories is generally young, female and unskilled. Mucn of the time the individuals represent new additions to the labor force rather than a return to work of those who had been idled. As a result, unemployment may not significantly decline.

Another basic distinction between the United States economy and those of the export-led developing areas is the different role of the consumer. In the United States the worker is viewed as both producer and consumer and wages earned in one capacity serve to stimulate mass demand for goods and services.

In the export-led economy the worker is viewed primarily as a factor of production. Wages are kept low to encourage continued export industry growth and little or no development of a mass consumer market occurs. The principal growth in consumer goods consumption that takes place in such areas is via the production or import of luxury goods for the handful of elite who operate the factories or profit from them.

My views on export-led development stem not merely from reading or from theory, but from personal experience as well. Two weeks ago I returned from a visit to the Far East where I served as an advisor to the U.S. delegation negotiating textile agreements. Among the countries we visited was Bangladesh. My colleagues and I were deeply moved by the abject poverty we found there and would like to help those unfortunate people. Yet, I was also deeply impressed with the price extracted from the country and its workers by foreign firms which have encouraged the establishment there of export-only plants.

Bangladesh apparel plants produce on two levels. On the one hand they serve as contractors for manufacturer-exporters in the Big Three exporting countries -- Hong Kong, Korea and Taiwan. Fabric is brought in under bond, apparel is produced from the imported fabric and the finished goods are shipped back to either the Big Three or to their customers. On the other level, sales are made directly to U.S. retailers or importers. In this case, the Bangladeshi manufacturer himself pays for the fabric. In both circumstances, none of the finished product is permitted to enter the domestic market.

It was obvious to us that the Bangladeshis were being ripped off by their customers. In one plant I visited, men's dress shirts were being made for export to the U.S., the U.K. and West Germany. The local plant was paid about $27 a dozen, or about $2.25 each, for the completed shirts. The shirts were preticketed with price tags for use in the importing countries' stores; they approximated $16 each after currency conversion -- more than seven times the amount paid the Bangladesh factory.

This pricing pattern is not unique to Bangladesh. I was exposed to a similar situation earlier this year on a visit to Indonesia. In one typical plant I was shown designer jeans made for a prominent American brand name that retail here for $40 to $45. The Indonesian manufacturer was paid $5 a pair!. The same plant also produced a women's garment for a major chain. The manufacturer was required to put a retail price tag of $9.95 inside the cellophane wrapper. He received $1.20 to cover his costs and profit as well as a commission to the agent who got him the work.

The local manufacturers who are underpaid for their work pass along the largest part of their burden to their workers so as to maximize their own returns. In the Bangladesh plants I visited, wages reportedly varied from 900 to 1200 taka a month for a six day, 10 hour per day schedule. In U.S. terms this worked out to between $28 and $37 a month or from 10.4 to 14 cents per hour. These abyssmal wage levels apply to experienced workers; trainees received considerably less for the first three months of employment. Workers also received no compensation for an inflation rate estimated to be 15 to 25 percent a year; their real wages declined.

While in Bangladesh I also had occasion to exchange views with a leader of one of the country's labor organizations. He painted a picture that was even worse than what I had already heard. I was informed that the minimum wage in Bangladesh was less than the equivalent of 7 cents an hour and that the average sewing machine operator earned 11.8 cents per hour. When a factory had a rush order, I was told, the employer locked the factory doors and workers were forced to work around the clock. At peak periods, this can come to a work week of 70 to 75 hours. Workers are supposed to receive double for overtime work, but, I was told that it is rarely paid.

Trainees, I learned, are paid 100 to 150 taka or the equivalent of $3.08 to $4.62 a month. They are required to guarantee in writing, including those that are illiterate, to stay on at work after a three month training period. If they leave before they are released, they are required by the terms of their signed statement to pay the employer over 10,000 taka ($307), almost one year's pay. This form of indentured servitude is presumably illegal in Bangladesh and has been fought in the courts on a case by case basis.

Labor union activity cannot take place openly because of government attitudes and the martial law in effect.

My personal experiences abroad have been vivid evidence of the exploitation of Third World workers in the misguided belief that exports, to the exclusion of developing the internal economy, would lead to economic development. In all too many situations, the expected benefits have not materialized. One can count on the fingers of one hand the few countries where genuine develpment appears to have taken hold. Among them are Korea, Singapore and Taiwan. These areas, however, are in the minority. And in none of them did development spring exclusively from export-targeted apparel production.

The major factor encouraging the huge increases in apparel imports to the United States each year is the tremendous gap in wage levels between the U.S. and the Third World. While it is desirable to eliminate so-called unfair trade practices, this approach should not be viewed as a way to ameliorate the flood of apparel imports that is destroying American jobs.

APPENDIX A

HOURLY COMPENSATION * COSTS FOR PRODUCTION WORKERS, APPAREL PRODUCTS AND OTHER TEXTILE MANUFACTURING, 1984, U.S. COMPARED TO TWENTY LEADING LOW-WAGE APPAREL EXPORTING COUNTRIES **

Country	Hourly Compensation U.S. $	Index U.S.=100
United States	7.00	100
Taiwan (1)	1.39	20
Hong Kong	1.62	23
South Korea	0.86	12
China (2)	0.21	3
Philippines (3	1.54	22
Indonesia (2)	0.18	3
Singapore	1.74	25
Thailand (2)	0.46	7
India (2)	0.58	8
Sri Lanka (2)	0.23	3
Mexico (5)	1.00	14
Dominican Republic (4)	1.24	18
Malaysia (2)	0.35	5
Haiti (4)	0.43	6
Pakistan (2)	0.40	6
Bangladesh (6)	0.16	2
Macau (7)	1.07	15
Brazil (1)	0.89	13
Costa Rica (4)	0.86	12
Jamaica (4)	1.02	15

---

* Hourly compensation includes all payments to workers for time worked and not worked, the cost of payments in kind and employer contributions to legally required insurance programs and contractual and private benefit plans.

** Ranked according to U.S. apparel imports for year ending June 1985. These 20 countries accounted for 88.5 percent of total apparel imports for this period.

NOTES

(1) Est. based on ratio of 1983 hourly comp. in apparel to U.S. hourly comp. in apparel, applied to 1984 U.S. hourly comp. in apparel.

(2) Est. based on ratio of 1984 hourly comp. for spinning and weaving workers to comparable U.S. workers, applied to 1984 U.S. apparel hourly comp. For source, see ITC report, pp. 158, 215.

(3) Est. based on ratio of 1984 hourly comp. for textile workers to comparable U.S. workers, applied to 1984 U.S. apparel hourly comp. For source, see ITC report, p. 284.

(4) Est. based on ratio of reported hourly comp. for apparel workers to U.S. apparel workers, applied to 1984 U.S. apparel hourly comp. For source, see ITC report, p. 425.

(5) Est. hourly comp. for workers in in-bond factories along U.S. border. For source, see Business America article.

(6) Est. based on report in The Asian Labor Monitor.

(7) Est. based on textile and apparel wages relative to Hong Kong and Taiwan. See ITC report, p. 189.

SOURCES

U.S. Bureau of Labor Statistics, unpublished data, August 1985.

U.S. International Trade Commission, Emerging Textile-Exporting Countries, 1984, ITC Publication 1716, July 1985.

U.S. International Trade Administration, Mexico's In-Bond Industry Its Dynamic Growth, Business America, Nov. 26, 1984, p. 30.

Asian Monitor Resource Center, Bangladesh--Dramatic Growth of Garment Exports, The Asian Labor Monitor, June 1985, p. 17.

STATEMENT OF ROBERT F. EISEN, GREENWOOD MILLS, INC., NEW YORK, NY

Mr. EISEN. Thank you.

My name is Robert Eisen. I'm employed by Greenwood Mills, Inc., a privately owned textile company headquartered in South Carolina.

In a 3-year period from 1981 to 1983, we invested $135 million in modernizing our plants. In one of the units we built, we invested $120,000 per employee in fixed assets, which is a good barometer of the sophistications in the textile mill industry.

Earlier today, there was a lot of discussion on jobs. Before we invested the $135 million, we employed 6,000 people. When we concluded the investment, we employed 7,000 people. This refutes a statement that is made by a number of people that modernization is what is causing unemployment in the textile industry.

However, in 1983 and 1984, as the flood of imports came into the country, we had to let 2,400 people of that 7,000 work force go.

Our plants are very efficient. Some of our units are probably the greatest textile mills in the world.

On a level playing field, I think in almost all areas we can compete worldwide. But we are not on a level playing field. We have heavy subsidies being paid by almost all of the oriental countries, the exceptions being Japan and Hong Kong. However, in these countries there is prima facie evidence that massive transshipments have taken place.

If we are so competitive, why are we having a problem in the textile mill industry? Our suppliers of fiber are efficient. The cotton farmer in this country is great. He grows cotton efficiently. The sheep ranches raise wool, and that is done efficiently. And the manmade fiber producers are probably the most efficient in the world. So we are getting our raw material, at the right price levels. Why can't we compete?

A high percentage of our fabric is sold to the apparel industry. To automate an apparel plant is extremely difficult. There are some beacons out there of light. One of the large shirt companies sent $16 million modernizing plants, and they can produce dress shirts here in this country below the landed cost from the Orient. There is also a women's and children's wear manufacturer who has a very efficient unit, with eight work stations producing sophisticated garments. But these are all in-house produced automated machines, and they are not generally available to his competitors.

If the garment industry is finding it difficult to compete, we in turn lose our customers. We can have the greatest plants in the world, but we can't compete.

And why can't we compete? Why can't we ship abroad? There's a book 251 pages thick published by the Department of Commerce. It is entitled "Foreign Regulations Affecting U.S. Textile and Apparel Exports." Nineteen pages in here are on Korea.

I am a member of the Department of Commerce Management-Labor Textile Advisory Committee. I've been an industry advisor on a number of the bilateral agreements. On one of the bilateral negotiations with South Korea, I said we want to open the South Korean market up; we want to ship there. The gentleman from our

Government in the trade negotiator's office said that's not our job. So I said, well, whose job is it? There was no response.

Senator CHAFEE. In other words, your pitch is a little bit different from Mr. Starobin's in that you would be satisfied, I gather, if you had equal access into the Korean market that they have here. Is that right?

Mr. EISEN. If we had access to foreign markets, we could obviously ship abroad and export.

Senator CHAFEE. Well, I agree with what you are saying. Why don't you just conclude?

Mr. EISEN. OK. The conclusion I would make is this: The manufacturing base in this country, starting with Henry Ford in 1914, when he paid $5 a day as a wage level, which was substantially above the going market, created the middle class in the United States with disposable income. And the manufacturing industry is getting wiped out because countries with lower wage rates and illegal subsidies are penetrating our market, and they are taking it away from us.

Senator CHAFEE. All right.

Mr. Mack.

[The written statement of Mr. Eisen follows:]

STATEMENT ON U.S. TRADE POLICY

BY
ROBERT F. EISEN
GREENWOOD MILLS, INC.
111 West 40th Street
New York, New York 10018

THE UNITED STATES SENATE
FINANCE COMMITTEE
November 20, 1985

My name is Robert Eisen. I am employed by Greenwood Mills, Inc., a privately owned textile company headquartered in South Carolina. In a three year period from 1981 to 1983 we invested $135 million in modernizing our plants to protect our share of market, our investment, and the jobs of our employees. Prior to this expenditure, we employed about 6,000 and afterwards 7,000. I cite these payroll figures to refute statements that the loss of jobs in the U.S. textile mill industry is due primarily to modernization and to a lesser extent to imports.

We believe Greenwood Mills' plants are among the most modern textile mills in the world, and that the American textile industry is the most efficient in the world. All of the fibers that Greenwood Mills consumes are produced in the U.S.A. In addition, we do not import any textile products. Our customers are assured that all of our fabrics are made in the U.S.A. I mention this by way of background so that you can properly evaluate my comments.

The American cotton farmers and wool growers are efficient, and the U.S. man-made fiber producers are the most efficient in the world. If the U.S. textile mill industry is without a peer, and its fiber suppliers are efficient, why do we have a severe problem with imports?

The U.S. textile mill industry on a level playing field could be competitive worldwide in almost all product areas. However, our industry is part of a larger soft goods complex. Many of our customers fabricate apparel, home furnishings and industrial products from our fabrics. The U.S. apparel industry was and possibly still is the largest customer for our industry. However, because of the nature of their product, it is difficult to automate an apparel plant. Although there are a few apparel units in this country who can compete against foreign suppliers, the vast majority cannot. Labor rates in many of the exporting countries are less than the equivalent of $1.00 per hour and in the case of the Peoples Republic of China $.16 per hour. Most foreign apparel plants are inefficient by American standards and even with labor rates substantially below the U.S. would only be marginally competitive. Therefore, most of the low wage exporting countries employ export subsidies to gain a larger share of our market, with these subsidies in some instances being as high as 60%. In addition, there is prima facie evidence that massive trans-shipments took place to subvert our quota system.

Our government has no trade policy and has been lax in administering the bi-lateral textile agreements. As a result, in 1983 textile and apparel imports increased 32% to record breaking levels, and in 1984 increased 25% over 1983. These imports were devastating with many apparel, textile and man-made fiber plants closing. Greenwood Mills, with its modern plants, was forced in 1984 and 1985 to let go 2,400 employees. If the U.S. apparel industry disappears, there will be little or no U.S. textile mill industry and no U.S. man-made fiber industry.

Many of the foreign markets are closed to our products with these restrictions imposed by the very same countires who are demanding a larger share of our market.

Henry Ford in 1914 announced that he would pay his workers $5.00 per day, a wage scale substantially over the going rate. He helped create a middle class with disposable income so that they could buy automobiles and other products. Other manufacturers followed his example. For 71 years American manufacturers, with their payrolls and wage scales, have been the primary force behind creating this great American market. Is our government going to sit idly by and watch low wage foreign countries, many of whom are using illegal export subsidies, take away our market and the jobs of American citizens?

It is my understanding that in 1978 the U.S. Congress suggested that U.S. government personnel in embassies and consulates abroad, should be alert for illegal trade practices prevailing in the country in which they are stationed and should forward this information to Washington, D.C. so that it could be published and made available to interested American industries. In addition, under our trade laws, the U.S. government has the authority to bring counter-vailing suits against foreign governments engaging in illegal export subsidies. To my knowledge the Administration has not gathered any information on illegal trade practices, nor published any such information, nor brought any counter-vailing suits for illegal export subsidies. Why?

When the Multi-Fiber Arrangement on textiles was renewed in 1982, the European community, in negotiating their bi-lateral agreements, imposed rollbacks on shipments in sensitive categories from key suppliers. As a result this put increasing pressure on our market resulting in the substantial increases stated above.

Recently Japan imposed unilateral rollbacks on textile and apparel shipments from China, Taiwan, South Korea and Pakistan.

In spite of what the European community and Japan have done, the Administration still insists on a policy of no rollbacks. Why?

An example of a lack of a trade policy is the Administration's handling of Indonesia. This country was not a supplier of textiles and apparel to the U.S. until 1980 when they shipped a modest 7 million square yard equivalent. In 1981 this increased to 14 million square yard equivalent. In 1982, with shipments increasing substantially, the Administration negotiated at mid-year a three year bi-lateral agreement. 1982 imports were 42 million square yard equivalent. In 1983 they shipped 114 million and in 1984 -- 268 million square yard equivalent. To make these hugh increases legal, it was necessary for the Administration to amend the bi-laterial agreement three times. In mid-1985 the Administration negotiated a new three year bi-lateral agreement with Indonesia starting with a base of 285 million square yard equivalent. How did Indonesia reciprocate our generosity? They waited about a month and then bought 220,000 bales of Chinese cotton because it was cheaper than the American cotton they had been using.

Our trade negotiators only know how to give away our market. They get nothing in return.

STATEMENT OF MR. JAMES H. MACK, PUBLIC AFFAIRS DIRECTOR, NATIONAL MACHINE TOOL BUILDERS' ASSOCIATION, McLEAN, VA

Mr. MACK. Thank you, Mr. Chairman. We appreciate the opportunity to address the committee about the interplay between national security and trade practices, both foreign and domestic, fair and unfair.

In many respects, national security considerations transcend the traditional debate between free trade and fair trade and protectionism. That's so because no obligation of the Federal Government is more important than the protection of our national security.

Therefore, our Government quite correctly imposes very severe controls on the export of items, such as machine tools, which are likely to make a substantial contribution to the military capability of potential adversaries.

Well, Mr. Chairman, if it's important enough to keep critical technology out of the hands of the Soviet Union, then it ought to be important enough to keep it in the United States. And that's why Congress enacted back in the 1950's section 232 of our trade laws—the national security clause. Our testimony outlines the devastating effects that imports have had on the machine tool industry, and we are convinced, on the national security of the United States.

In March 1983, the National Machine Tool Builders' Association filed a petition under section 232 with the Secretary of Commerce. And under that statute, he has a year within which to make a decision. In response to our petition, the Commerce Department conducted a probing investigation of the facts and concluded that the continued displacement of U.S. machine tool production capacity by imports is a clear threat to the national security. Secretary Balridge sent his recommendations for action to the White House on February 28, 1984.

His recommendation is supported by the Defense Department, by over 200 Members of Congress, including many from this committee. Yet for almost 21 months, no action has been taken. The staff of the National Security Council has prevented this matter from even being considered by the President.

When we filed our petition, we predicted that if prompt action wasn't taken, imports would increase substantially, U.S. production capacity would wither, and more and more U.S. companies would begin sourcing offshore. Action hasn't been taken, and our predictions have come true. Indeed, in many respects, they have been surpassed.

Imports continue to grow. They now account for more than 40 percent of domestic machine tool consumption. The most vulnerable domestic markets continue to be numerically controlled machining centers and turning machines, two high-tech and defense-sensitive machine tools which are vital components of flexible manufacturing systems and factories of the future that we are all hearing so much about.

Mr. Chairman, action must be taken before this debilitating trend becomes entirely irreversible. And we strongly urge your passage immediately of legislation, S. 1679, introduced by Senators

Grassley and Heinz and Proxmire and Moynihan and seven other Senators, providing a 90-day deadline for——

Senator Chafee. Well, that's in the legislation we are going to introduce this afternoon.

Mr. Mack. I'm aware of that, Senator, and we are very appreciative of that.

Senator Chafee. Good. Why don't you get on with what else you would like.

Mr. Mack. Well, we urge you to pass that legislation as quickly as possible. We think that what is at stake is not only the welfare of one industry, but the security of our country which rests on a prompt resolution of this issue.

We think that future deadlines are essential if other defense-related industries are not to avoid the costly and unwarranted delays that we have experienced. The current situation is, in effect, a trap for the unwary. It's clearly inconsistent with the legislative intent of the national security clause since continued inaction results in further erosion of our defense base. And we urge your immediate consideration and adoption, Senator, of that legislation which you indicate that is going to be included in the trade package that you are introducing this afternoon. We appreciate your help.

Senator Chafee. OK, fine.

[The written statement of Mr. Mack follows:]

STATEMENT BY
JAMES H. MACK
PUBLIC AFFAIRS DIRECTOR
NATIONAL MACHINE TOOL BUILDERS' ASSOCIATION
BEFORE THE
COMMITTEE ON FINANCE
UNITED STATES SENATE
NOVEMBER 21, 1985

Good morning. I am James H. Mack, Public Affairs Director of the National Machine Tool Builders' Association (NMTBA), a trade association whose membership accounts for approximately 85% of United States machine tool production. Mr. Chairman, NMTBA commends your initiative in convening these hearings to examine appropriate legislative responses to the realities of global competition. Certainly your inquiry is a timely one.

We appreciate this opportunity to address the Committee regarding the interplay between national security and trade practices -- foreign and domestic; fair and unfair. I'll begin by noting, however, that, in many respects, national security considerations transcend the traditional debate between "free trade" vs. "fair trade" vs. protectionism. No obligation of the federal government is more important than the protection of the national security.

The machine tool industry is critically -- indeed, uniquely -- important for national defense. The products and technology of this industry are the essence of the industrial manufacturing process: they are, by definition, the "tools" of production. As such, machine tools are needed to produce every ship, plane, tank, missile, transport vehicle and other armament used by our armed forces, as well as essential elements of the supporting civilian infrastructure. Many armaments are extremely sophisticated and require machine tools of the highest technological level.

Machine tools are therefore fundamentally different from specific end-products used for defense because they are the prerequisite for the production of virtually all such products. Machine tools are, in short, the cornerstone of the industrial base supporting our national security.

Because machine tools are recognized as essential to military production, export controls imposed for purposes of national security have a direct and often substantial impact on our members' ability to export much of the equipment they manufacture. Indeed, more than half of the world market for machine tools -- outside of the U.S. -- lies in Communist bloc nations -- a market which is, in effect, foreclosed to U.S. machine tool manufacturers.

NMTBA recognizes that our nation's ability to maintain a defense-industrial edge over its potential adversaries is absolutely essential. That is why we continue to oppose any trade-related activity which would permit our adversaries to significantly and directly increase their military capabilities.

When the Export Administration Act came up for re-authorization in 1983, we, along with others in the business community, suggested ways in which the Act could be more effectively and realistically administered. A number of those reforms were finally adopted earlier this year.

Certainly, if it is important enough to keep critical technology out of the Soviet Union, it is important enough to keep it in the United States. Yet, ironically, while we spend considerable resources to deal with the former problem, the latter has received far too little attention. Imports of sophisticated machine tools -- often subsidized -- have dealt a devastating blow to the domestic machine tool industry. Many machine tool manufacturers are either leaving the business, moving their operations offshore, or becoming distributors of foreign-made products. The result is a rapid deterioration of our domestic capacity to produce significant quantities of technologically advanced machine tools.

Thus, when President Reagan met Chairman Gorbachev at the summit, his job was made considerably more difficult in light of the fact that, over the past few years, the Soviet Union has made dramatic improvements in its industrial base -- while America's has been shrinking. Even though we've spent billions for defense, our nation is less secure today than it was three years ago because the industrial base that it required to sustain America's defense establishment has been decaying. We are relying on this decaying base to sustain and equip our forces in time of emergency, to rebuild the nation when the emergency passes, and to stand as a strong deterrent to potential aggressors who would test the "Arsenal of Democracy."

According to defense experts, including Defense Secretary Weinberger, the Soviet Union has been aggressively upgrading its industrial base and dramatically improving its strength. The Soviet "machinery sector continues to realize the most rapid growth in the economy," according to Soviet Military Power in 1984, a publication of the U.S. Department of Defense.

American industrial experts who visited the Moscow International Machine Tool Exhibition 18 months ago were astounded by the Soviet's technological progress. They reported that the Soviets have become world-class machine tool producers. They also witnessed dramatic advances in the industrial technology used in Soviet factories, versus the obsolete equipment used only five to ten years earlier.

For example, the USSR's Krasny Proletary Machine Tool Factory is reportedly the world's largest lathe manufacturer. In one location, its 4,000 workers produce more than 1,000 quality lathes per month (compared to total U.S. production of less than 300 per month). In the fall of 1984, a new, fully automated, robotized plant increased monthly production by 800 advanced-technology, computer-controlled lathes. This plant, and others like it, are enhancing the USSR's conventional defense capabilities at a time when America's machine tool industry has shrunk 25% and is continuing to wither at an accelerating pace.

In March 1983, our industry voiced its concern by notifying the Administration of the threat posed to our national security by the demise of vital machine tool capacity. The industry's request for temporary import relief has been described as the strongest case ever submitted under the National Security Clause (Section 232) of the Trade Expansion Act of 1962.[1] While the Association has long been a proponent of free trade and has one of the most active international trade promotion efforts in the trade association field, we cannot stand idly by while key segments of the American machine tool industry are decimated by targeted sales of foreign machine tools -- and, more importantly, while the national security of the the United States is imperiled by the transfer of machine tool productive capacity to the Far East.

One could debate forever the importance or desirability of protecting the domestic production capacity of individual American industries. But the importance of a strong U.S. machine tool industry to our national security is irrefutable. No responsible person would argue that it is possible to build armaments and infrastructure without machine tools. And no thinking person would want to rely on our ability to transport sufficient quantities of multi-ton machinery over thousands of miles of ocean during wartime (nor, for that matter, to keep foreign machine tool factories from being destroyed by an adversary), should America become dependent upon foreign sources for its fulfillment of its machine tool needs.

---

[1] NMTBA appeared before the Committee in 1983 to discuss the industry's request for temporary import relief. See, Statement by James A. Currie, President, Erie Press Systems (representing NMTBA), Before the Committee on Finance, U.S. Senate (98th Cong., 1st Sess.), October 3, 1983.

In response to the industry's Petition, the Commerce Department conducted a probing investigation of the facts and concluded that the continuing displacement of U.S. machine tool production capacity by imports is a clear threat to national security. Secretary Baldrige sent his classified recommendation for action to the White House on February 28, 1984. Secretary Baldrige's position is supported by the Defense Department and by over 200 members of Congress, including many on this Committee.

Yet no action has been taken. The staff of the National Security Council has prevented this matter from even being considered by the President.

When we filed our Section 232 Petition, we predicted that, if prompt action was not taken, imports would increase substantially, U.S. production capacity would wither, and more and more U.S. companies would source offshore. Action has not been taken; and our predictions have come true. Indeed, in many respects they have been surpassed. Imports continue to grow -- they now account for more than 40% of domestic machine tool consumption. The most vulnerable domestic markets continue to be numerically controlled machining centers and turning machines -- two "high tech" and defense-sensitive machine tools which are vital components of flexible manufacturing systems and "factories of the future" that we are all hearing so much about.

And although the machine tool market gained some momentum during 1984, that surge has not carried forward into 1985. Orders are down 11% for the first three quarters. Shipments are up 11% over 1984, but this meager increase is unlikely to be sustained in the face of weakening orders.

It should be recognized that the significance of the threat of machine tool imports goes far beyond the welfare of just the domestic machine tool building industry. If the industry is allowed to be overwhelmed by foreign products, the innovations and new manufacturing industries will be lost. Foreign firms will then have the upper hand in the development of new technology and will be the leaders in the drive to more efficient, lower-cost production of manufactured goods. The loss of American's machine tool building capability could well signal the beginning of the decline for all of America's metalworking manufacturing industries.

Action must be taken before this debilitating trend becomes entirely irreversible. We strongly urge your passage of legislation (S. 1679) introduced by Senators Grassley, Heinz, Proxmire, Moynihan, and seven other Senators providing a 90 day deadline for Presidential decision-making in future 232 cases and mandating a positive finding in the machine tool 232 case, unless the President successfully negotiates a VRA with Japan. As the sponsors of the legislation have recognized, a delay of almost two years is unconscionable -- with each passing day, the threat to our national security posed by machine tool imports grows more pronounced. It is not only the welfare of one industry, but the security of our nation which rests on a prompt resolution of this issue.

We believe that the imposition of a deadline on Presidential action in future 232 cases is essential if other defense-related industries are to avoid the costly and unwarranted delay experienced by NMTBA. The current situation -- in effect, a trap for the unwary -- is clearly inconsistent with the legislative intent of the National Security Clause, since continued inaction results in further erosion of our defense industrial base.

It should be noted that the 90 day time limit is imposed after the Secretary of Commerce has, under the current statute, a full year within which to complete his investigation and submit a recommendation to the President. By ensuring that 232 cases will be evaluated in a manner which truly reflects the urgency of the National Security Clause, the imposition of a deadline can only serve to improve national security.

Mr. Chairman, I wish that I could be more positive, but the facts dictate otherwise. On the bright side, the industry is determined to survive -- and survive it will. But the process of survival for many is likely to include a transfer of more productive capacity and jobs offshore. The Administration's failure to act in a timely fashion on our National Security Import Relief Petition has produced this result -- which, in our opinion, poses a dangerous threat to America's ability to mobilize against or to deter Soviet aggression. Thank you. I would be happy to respond to your questions.

Senator CHAFEE. Now, Mr. Mack, I noticed in an article by Mr. Edson I. Gaylord, chairman of the board and president of Ingersol, which he points out is one of the largest machine tool companies in the country, although private, he doesn't seem to have the concern for protectionism that you do.

Mr. MACK. Well, Senator, I've read Mr. Gaylord's statement.

Senator CHAFEE. Is he a member of your organization?

Mr. MACK. No. He is part of the 15 percent of the industry that are not members of the National Machine Tool Builders. From time to time joins and withdraws over various matters.

I've read his statement. It's a very persuasive statement on the point of what the domestic machine tool industry needs to do to become a vibrant industry. You and I have had this discussion in the past, and that is precisely what needs to happen.

Senator CHAFEE. What's needed are managers, the people, the spirit, the technological competence, the ability to mass produce, the ability to move raw materials.

Mr. MACK. Senator, I think we are not in disagreement as to what is needed. The question is, how do you get from here to there? We are suggesting to you that what is happening in the real world with good management, with the fact that 75 percent of the products that American machine tool builders are selling today weren't even in existence 5 years ago; with the fact that Business Week magazine recently reported that our industry's investment in R&D was growing faster than everybody else except for computer software. With all of that, unless something is done to curb the influx of imports, more and more companies are going to do as Mr. Gaylord has done, which is to source products offshore and bring them into the United States. That's fine. That makes good economic sense for that company and for other members who are doing precisely that—many in your State.

That makes good economic sense. From the standpoint of the national security of the United States, however, which is what our petition is all about, it makes terrible sense, because we are putting ourselves at the mercy of being able to transport vitally needed machine tools if—God forbid—we ever get into a mobilization, across 7,000 miles of ocean. How you guarantee that or guarantee the existence of those foreign sources, if we become dependent on them, in the event of a national emergency is beyond me.

Senator CHAFEE. OK. Mr. Eisen, if U.S. textile producers are as efficient as you pointed out, why have the textile imports increased at such a tremendous level?

Mr. EISEN. Heavy subsidization.

Senator CHAFEE. You think that's it? You mean in the competing countries?

Mr. EISEN. Taiwan, South Korea, the larger shippers of fabric from the Orient, they are subsidized. And they have very sophisticated subsidies.

The administration has the authority granted to it by Congress to file countervailing duty actions against foreign governments for illegal subsidies, but the administration refuses to do it.

Senator CHAFEE. All right.

Mr. Starobin, in light of your testimony—and you've dealt particularly on Bangladesh—what should the United States do?

Should we limit imports from countries with these extremely low wages?

Mr. **Starobin**. Senator, the kind of economic development that's taking place in Bangladesh is something that we have urged on that country and on other countries. I think we have urged a very mistaken policy. It's a policy that does not benefit the internal economy. I think that policy should be reversed, if we have any genuine interest for the poor people in these countries.

Senator **Chafee**. Judging from what you said about the price tags that are put on the shirts, are you suggesting the consumer doesn't get any benefit out of this?

Mr. **Starobin**. I am suggesting that very definitely, sir. And my testimony goes on to talk about an experience I had in Indonesia at the beginning of this year. It's a rather universal phenomenon in which the workers are being ripped off, the manufacturers in these countries are being ripped off, and the only ones who benefit are the importers and retailers. They mark up——

Senator **Chafee**. You mean in the United States?

Mr. **Starobin**. In the United States. And in the United Kingdom and in West Germany, except they place greater restrictions on their imports of apparel than we do.

Senator **Chafee**. What would you do if you were us? Each of you gentlemen, briefly. Each comes in here and says we have got to restrict A, B, and C—machine tools, apparel, textiles. And pretty soon, where are we? Aren't we restricting everything? What wouldn't we restrict? Steel? You heard Mr. Bieber from the automobile companies before. His people are getting paid $25, with fringes, an hour. Restrict the automobile imports. So how is this any different from what we did in the late 1920's and early 1930's?

Mr. **Starobin**. I think there is a great difference, Senator.

Senator **Chafee**. We passed the Smoot-Hawley tariff.

Mr. **Starobin**. I think there is a great difference in that trade plays a much more important role than it did in the 1930's.

I would argue that this is a much more complex problem than has been presented this morning. I think the problem relates to a whole series of factors. We allow 1 million people into our country each year, at least legally and illegally, without providing for jobs or job opportunities for them. I would argue that the primary responsibility of each nation-state—and every nation-state practices this except ourselves—is to protect its own people. Once it has done that, fine; there is the rest of the world. But its primary responsibility is to its own people.

Senator **Chafee**. All right.

Mr. **Starobin**. And the great success of Japan is that it has done precisely that.

Senator **Chafee**. All right. OK—fine. Well, thank you all very much. I appreciate your coming.

And the next panel will be Mr. Iverson, Mr. Thornton, and Mr. Freeman. Oh, Mr. Iverson has had to go so we will have Mr. Thornton and Mr. Freeman. Gentlemen, if you will start right off. Mr. Freeman, why don't you plunge ahead. You are here. Are you the only survivor?

Mr. **Thornton**. I'm here.

Senator **Chafee**. You are here. OK. Go ahead, Mr. Freeman.

STATEMENT OF HARRY L. FREEMAN, EXECUTIVE VICE PRESIDENT, AMERICAN EXPRESS CO., NEW YORK, NY

Mr. **Freeman**. Thank you very much. I'm Harry Freeman, executive vice president of the American Express Co. and vice president of the Coalition of Service Industries, which represents service exporters in the United States.

On the basic question, can service sector companies from the United States compete in the world market in a regime of basically fair trade—the answer is most emphatically "yes." I think most service companies in the United States in the last couple of years have gotten very lean and mean and very competitive—whether in the banking, insurance, or investment businesses, or in firms employing architects, engineers, or lawyers. All of those industries have gotten very efficient. They can take care of themselves around the world if they have a fair trade regime.

Second, do we have a fair trade regime? In some areas, yes; in some areas, no. As I get off the subway every morning in Manhattan, I go down Wall Street. Three of the last three offices I see before I hit the American Express headquarters, are the Dresdner Bank, the Commerze Bank and the Deutsche Bank. Two months ago in Frankfurt, when I went to the headqauarters of Deutsche Bank, it was somehow a very different situation—I didn't see foreign banks on my walk to their office.

We have a deteriorating situation in trade-in services. The good news, I believe, is the United States is very aggressively tackling the problem:

First, the trade bill which was passed last October—with your help, Senator—was terrific. It gave us remedies that we didn't have before. We are now respectable; we are in out of the cold.

Second, the GATT is moving toward some very serious, very tough negotiations in Geneva. I see today's paper reports that we are having a lot of trouble getting services on the agenda, and we may push for another formal vote in Geneva. And if we have to, I think we should. I think the U.S. position is absolutely right, and the few countries that are against us, I just think are wrong. If we don't move to have a regime in services in the next couple of years, services will then go the way of the other industries we have heard this morning—automobiles, shoes, and textiles.

Those industries have very, very major problems. Services haven't gotten there yet, but I deplore the attitude of those who say, "Put services off; they aren't that important". We will get to them at some remote forum, at some remote time. That is not the thing to do.

On the points that were discussed earlier by Commissioner Norwood, particularly.

The main statistics I would like to leave with you are these: Per capita income in the United States has gone up 25 percent in the last 10 years. During this time, the number of manufacturing jobs has been in absolute decline, while 90 percent of the new jobs have been in the service sector. It follows that those services jobs must be, on the average, reasonably higher paying than the manufacturing jobs. It cannot be otherwise.

Senator **Chafee**. Well, thank you. Did you finish?

Mr. **Freeman**. That's it.

Senator **Chafee**. OK.

[The written statement of Mr. Freeman follows:]

STATEMENT

of

Harry L. Freeman
Executive Vice President
American Express Company

Good Morning, Mr. Chairman and members of the Committee. My name is Harry L. Freeman and I am an Executive Vice President of American Express Company and the Vice President of the Coalition of Service Industries. I am very pleased to have the opportunity to appear before the Committee today to discuss the ability of U.S services firms to compete abroad.

Mr. Chairman, it has been well over a year since my last appearance here. Since that time, you Mr. Chairman, members of the Committee and your colleagues in the Senate and in the House, have enacted landmark legislation that puts services on par with goods, provides U.S. exporters of services with strong remedies against unfair trade practices, and establishes negotiating objectives with respect to services. The importance of the Trade and Tariff Act is yet to be fully realized, but we are beginning to see how it will be utilzed. As a result of this new law, for example, the U.S. Government has recently brought a trade action against the Korea for that country's barriers to foreign insurance firms. I am also aware that some of the members of this Committee have communicated concern to the U.S. Trade Representative's Office about West German restrictions on transborder data flows. As a result of your efforts, U.S. service providers are in a much better position than we were a year ago in terms of legal remedies for unfair foreign trade practices. After decades of being left in the cold, service exports have now achieved respectibility.

The service sector, which now accounts for fully 69% of the domestic product and around 25% of all U.S. exports, cuts across a wide array of businesses with varying interests. The Coalition of Service Industries is comprised of 28 service companies respresenting a broad cross section of industries. Our membership currently includes insurance companies, accounting firms, banks and financial services companies, food services, communications firms and others. My own Company is engaged in a variety of financial and travel-related services. Our businesses include our charge card services, travellers cheques, insurance, travel, data processing, financial planning, investment banking, international banking, brokerage and asset management services.

For the last ten years the U.S. has consistently run an overall trade surplus in services. That surplus, however, has declined dramatically over the last few years. The reasons for this trend vary. One reason, of course, has been the relative strength of the dollar to other currencies. Another major reason has been the growing proliferation of non-tariff barriers to U.S. service exports. The U.S. Trade Representative's recently released report on national trade estimates includes an extensive list of services trade barriers.

Another reason for the decline in the services surplus is increased competition. In our view, foreign competition is something that U.S. services firms must learn to live with. The fact is that anyone wishing to compete in the world markets must be tough and lean, and I am confident that most American services firms can meet and beat the foreign competition in a fair fight.

That gets us to the question at hand: whether U.S. service firms can compete with "fair" trade. I would submit that the answer is an emphatic yes. I think that our track record speaks for itself. Some of our service exporters - banks, insurance companies, investment firms and engineering firms - have become lean due to keen domestic competition and can, as a result, compete in a fair trade environment. Some examples:

- Because of deregulation and advanced information processing capabilities, U.S. banks are among the most efficient in the world.

- The same is true of U.S. stockbrokers and asset management companies.
- U.S. lawyers, accountants and management consultants are in a class by themselves.
- U.S. commercial food services and hospital management companies are also highly competitive.

U.S. competitiveness in services abroad stems from competitiveness in U.S. markets. After all, only the U.S. has over 17,000 banks - most countries have no more than a dozen.

The problem is that what we are dealing with is not always fair trade. We are increasingly finding ourselves trying to compete in a "managed trade" environment or in an environment rife with other unfair restrictions. For example, American asset management services can thrive in the European countries that afford us national treatment in financial services. Yet, in Canada, where foreign banks are limited to an aggregate share of no more than 16 percent of domestic assets, U.S. activities are necessarily inhibited.

Our desire to compete "fairly" with foreign countries is the motive behind U.S. exporters in seeking a GATT regime on services. Because many U.S. services enjoy competitive advantages, the U.S. cannot allow for a trade structure which puts us at a disadvantage in those areas.

Let me now turn to the upcoming GATT round. As we - both American Express and CSI - see it, next week will be crucial in determining how services will fit in the next round of trade negotiations. Based on the information we received from our friends in Geneva, and particularly from the media, we get the impression that the United States is frequently the sole protagonist for an agenda including services, while Brazil and India and three other developing countries are the opponents of the United States. The United States should not be the sole country that is in the forefront of pushing for services to be included in a GATT round. Sweden, the EEC, Canada and Japan have all been very supportive but need to be more vocal about it. Just last week I spoke before the Swedish Coalition of Service Industries to push this very point.

We are very proud and supportive of the United States Government's aggressive posture on the issue. Ambassador

Yeutter has been quite clear about his plans to pursue services negotiations and we are confident that services will be included in the upcoming GATT round on some substantive basis.

It may be that the service negotiations will be in fact prolonged over a period of years. That's fine so long as the result is a good agreement. Frequently, ongoing substantive negotiations are a better temporary deterrent to new trade barriers than a hastily agreed upon code of conduct, so long as the code eventually does emerge.

We also think that, with due respect, the developing countries in opposition have a position which is not well founded.

Their argument is for breaking off services from other issues. It seems to us that their interests would be in increasing access to developed country markets through linkage in the negotiations. A very recent editorial in The Economist of October 12, 1985 addressed LDC concerns quite well. That editorial which argued vigorously - and brilliantly, I believe - that services are a vital part of a GATT round and all of the world, including the developing countries.

The basic argument The Economist asserts is this: What is good for the United States economy in general is good for world trade, which in turn is good for every country; that the United States has almost reached the point where it cannot import more unless it exports more; and therefore building its exports of services is a good place to start; and trade liberalization would facilitate that. The Economist dismisses the concern of developing countries by arguing that the main areas of impact would be on the developed countries, that "national treatment" is fair and much preferable to any bilateral arrangement or principle of reciprocity.

As The Economist states: "In next month's annual meeting of GATT, developing countries should not cut themselves off from the best in accounting, insurance and banking because they think America's cry for freer trade in services means that only America stands to gain."

There is a notion that existing trade problems should be dealt with prior to any discussion of services. The argument goes that adding services to the agenda would be detrimental to handling of the tougher problems, and hence postponement of discussions on services (or reference to some other world agency) is in the world's interest. This myth assumes that

GATT and its contracting parties have much less capacity to deal with these issues than is the reality. Moreover, the trend towards increasing trade barriers to services is bad. With textiles, shoes, steel, and certain other goods, we have definitely moved to "managed trade". While I do not condone that status, I think the future for those goods lies in negotiations of quotas, allotments, and other aspects of a managed trade regime. Fortunately, in services we have an orientation to a freer trade regime, albeit one which is increasingly subject to deterioration. The task, then, is to address the deteriorating situation before it reaches the pathological state such as the commodities that I already mentioned. We should act now so that talks on services are not condemned to a remote forum at a remote date.

In summary, American Express and CSI are quite confident about the ability of the United States to maintain its competitive lead in the service sector. We look forward to working with the Committee in the upcoming months on efforts to more clearly define the goals we wish to accomplish in the GATT to assure fair trade in services. Thank you. I would be pleased to answer any questions.

STATEMENT OF LANEY THORNTON, PRESIDENT AND PRINCIPAL, SAN FRANCISCO MERCANTILE CO., DBA EILEEN WEST DESIGNS, SAN FRANCISCO, CA

Senator CHAFEE. Mr. Thornton.

Mr. THORNTON. Thank you. I'll try to be as brief as possible.

I'm Laney Thornton, cofounder of an American clothing manufacturer selling clothes under the name of my partner, Eileen West. We will sell about $14 million of clothes at wholesale this year. And I am proud to say that we manufacture all of our clothes in the United States.

In addition to sewing workers, we employ about 90 people directly in our company who design, purchase fabric, cut cloth, sell, and distribute our products. Our apparel is women's sleepwear, dresses, and sportswear in what I call the affordable, better clothes' price category, and we are sold at stores such as Bloomingdale's, Sak's, Woodies, Marshall Fields, plus many small shops and specialty stores nationwide.

When Eileen West and I founded the company in 1977, we imported all of our products from India for sale in the American market. Three years later, we shifted our manufacturing to the United States.

Retail stores in our particular market niche want to purchase high-quality clothes with very short leadtimes to take advantage of fashion trends. Consequently, now we buy fabrics, design our products, and cut them before sending them to numerous independently owned domestic sewing shops in San Francisco.

Because of our integrated operations and rapid response of domestic sewing operations, we can provide finished goods to retail stores within 2 months and less. Overseas, orders generally take 4 to 5 months.

Our progress speaks for itself since we have had 50-percent growth for the last 3 years in each year.

I want to make a comment on the current legislative issues involving textiles and apparel trade. I believe we could be seriously injured by further restrictions on the import of textiles. We purchase all of our fabric from American fabric convertors, companies that buy raw fabric from foreign and domestic mills and then print or dye the fabric to our specific order.

We cannot always obtain domestically the base fabrics that we need. We need a complex, broad range of fabric—delicate prints, plaids, cotton, silk, linens, and wools—for our range of products. Domestic mills make some, but not all of the fabrics in the limited quantities that we require.

I have talked to domestic mills, and they simply cannot produce the full range of fabrics that we need.

We compete in a very specific market niche. We constantly have to be flexible and make changes in our operations as necessary. Clothing merchandise is very fast moving and complex, and I do not feel that Government can possibly legislate effectively to deal with the many factors that influence our production.

I feel that industry-specific legislation can cause confusion and could be harmful in the long run. And as an example, I have here a garment that we produced. As you can see, it's an ornate garment. This is a dress that retails for about $150. As you can see, it has a lot of labor. It is made out of——

Senator **Chafee**. Dropped waist, is it?

Mr. **Thornton**. Very good. [Laughter.]

It's pleated, tucked. It's made of two different fabrics. This outside fabric is a linen, which comes from either Brazil or Romania. The lace all comes from the United States. And there is an inner garment here, a slip, that is a combed cotton lawn that is manufactured by Greenwood Mills, the company that just testified.

Senator **Chafee**. Mr. Eisen's company.

Mr. **Thornton**. That's right.

Senator **Chafee**. Good. He'll be pleased.

Mr. **Thornton**. We probably buy about a half a million yards a year from Greenwood Mills.

Senator **Chafee**. Do you buy anything from Cranston Print or VIP?

Mr. **Thornton**. Sure.

Senator **Chafee**. Excellent. You are a fine witness. [Laughter.]

[The written statement of Mr. Thornton and the statement of Mr. Iverson, Nucor Corp., follows:]

TESTIMONY OF
F. KENNETH IVERSON
CHAIRMAN AND CHIEF EXECUTIVE OFFICER
NUCOR CORPORATION
BEFORE
FINANCE COMMITTEE
UNITED STATES SENATE
NOVEMBER 20, 1985

Thank you for this opportunity to testify about our domestic steel industry.

We are a profitable steel company and are opposed to trade restrictions on steel products. We believe that tariff or non-tariff trade barriers delay modernization of our steel indsutry, cost the consumer billions of dollars and injure both our economy and smaller steel producers.

Basis of Comments

Nucor Corporation is a manufacturer of steel and steel products. We operate seven steel mini-mills on four sites. In 1984 we produced 1,500,000 tons of steel. We are the 9th largest steel company in the U.S. and have an annual capacity close to 2,000,000 tons.

1. All of our mills use the latest steel technology. 100% of our steel is continously cast.
2. For more than 12 years, the price of the steel products we produce, FOB our mills, has been equal to or less than the U.S. dockside price of these products from foreign suppliers.
3. For the last 15 years we have not closed a single operation nor laid off a single employee for lack of work.
4. We operate profitably. Since constructing our first steel mill in 1970 the company has never had a loss quarter.

Problems of the U.S. Steel Industry

There are two reasons why our primary steel industry has lost advantages it once had in the marketplace. One is that many of our steel plants are old and inefficient.

In the last three decades, most of the major developments in steelmaking were made outside of the United States. Our larger steel companies have not quickly accepted technological advances and have adopted new techniques only when the economic evidence was overwhelming.

Continuous casting is a method of producing a billet which can be rolled directly into a finished product. It eliminates ingot pouring, soaking pits, reheating furnaces and break-down mills. The yield from molten metal to finished product is significantly improved. It reduces energy costs.

Last year the U.S. produced about 39% of its steel by the continuous casting process. In Japan close to 90% of the steel was continuously cast. Italy, Austria, West Germany, Sweden, France, Canada, Belgium and the United Kingdom all had a higher percentage of continuously cast steel than we did in the U.S.

About 9% of the steel in the U.S. is still produced using old open hearth furnaces. The Japanese shut down their last open hearth furnace more than seven years ago.

The second problem of our major steel producers is productivity.

The May 3, 1985 issue of Iron Age Magazine lists the top 50 steel producers in the world for 1984. It also lists the productivity of these producers on the basis of tons per employee per year. The four largest U.S. producers averaged 320 tons per employee. The five largest Japanese producers averaged 462 tons per employee per year, almost 50% higher. The hourly rate of U.S. steelworkers has sometimes been blamed for the lack of competitiveness of the U.S. steel industry. It may be well to keep in mind that steel mill work is hard, hot, dirty, skilled and dangerous. In every industrialized country in the world, the steelworker earns more than the average manufacturing worker. In Japan the premium is close to 50%. The problem is one of productivity and not one of pay. The U.S. steel industry's problems in productivity stem from the outdated plants mentioned earlier and is aggravated by restrictive union work rules and an excessive number of people -- and here I include clerical, administrative and management as well as production workers.

Both of these problems have been well recognized and well documented.

Future of the Steel Industry

I am not pessimistic about the future of the steel industry. We have enough comparative economic advantages to have a steel industry that can compete in the international marketplace. We have an ample supply of iron ore and an ample supply of coke. Our electric costs are lower than those in most industrialized countries; we have low cost scrap, plus the advantage of lower freight costs in most areas of the U.S.

We have seen more realistic depreciation schedules, a reduction in corporate taxes and a relaxation of regulation. Our major steel companies are increasing the percentage of continuous cast steel and are modernizing their facilities.

The question is what can or should the government do to further facilitate and expedite this restructuring of the steel industry.

Areas to Help the Restructuring

We are opposed to tariffs or non-tariff trade barriers for steel products:

1. There are steel mills outside of the U.S. that can produce steel more economically than some mills in this country. They should not be denied access to our markets - or we to theirs.
2. Quotas and other non-tariff trade barriers have been tried before. There is little or no evidence to indicate that the steel quotas in the early 1970's or the trigger prices of the late 1970's had any beneficial effect in modernizing our integrated steel mills or making them more competitive in the international marketplace. They cause higher steel prices and delay modernization or closing of older, inefficient plants.
3. These barriers to steel imports cost the American consumer billions of dollars. There are estimates that the Trigger Price Program in the late 1970's cost the American consumer over a billion dollars a year and may have saved only temporarily some 12,000 steelworking jobs. That's over $80,000 per year per job.
4. The real hazard in trade barriers is that manufacturers outside of the U.S., or U.S. manufacturers who move outside, use the cheaper steel available on the international market and then ship into the U.S. a wide variety of products at lower cost than domestic manufacturers because of our higher steel prices. World market prices for some steel items are $100 to $200 per ton lower than U.S. domestic prices. This imbalance

will eventually have serious effects on the steel service center industry, the automotive industry, farm implements, appliances and numerous other industries where steel costs are important. With this occurring, steel demand in the U.S. will be lower and steel capacity would have to shrink even further. One steel analyst has projected that the Voluntary Restraint Program currently in effect will cause a decrease in the U.S. steel market of 1% per year through 1990 due to the increased imports of products where steel is an important component. It is ironic that tariffs and non-tariff barriers not only damage the economy but will accomplish the very thing they were designed to prevent.

We feel there are ways by which the government could provide assistance to the steel industry. Some of these include:

1. Programs for retraining or relocation are important for those employees affected by shutdowns.
2. Congress should not implement measures that reduce the incentive to invest in modernization or new technologies.

Protectionism for the steel industry will penalize the consumer, delay steel industry modernization, injure efficient steel producers, and could seriously damage the economy.

There are new technologies developing in the steel industry. By modernizing and by investing in these new technologies, our steel industry will eventually be able to compete in the international marketplace.

Senator CHAFEE. You sell to the upper end of the market. Would your same analysis apply to the lower- cost end? The K-Marts and Woolworths and other places? Would what you are saying apply there too?

Mr. THORNTON. I can't make a generalization about the entire market. The point that I'm making is that the apparel market is not just one market. It is many, many different markets. And we often get the feeling that the government in proposing legislation thinks that the marketplace is a single, undifferentiated market, much like automobiles, which is controlled by a few companies and very limited distribution.

I really would not comment on people in other market niches other than to say there are many, many market niches, and I believe in the strength of the American spirit to compete when the deck is not stacked against them.

Senator CHAFEE. OK, fine.

Let me ask Mr. Freeman a quick question. Do you think it's possible to have reciprocal legislation that would force these countries who traditionally have had a very tight banking system to open their banking system to the United States? Example: The Japanese can come to San Francisco and buy a bank. Do you think we should have reciprocal legislation that would say if they can buy a bank here, we ought to be able to buy a bank there?

Mr. FREEMAN. I think there ought to be universal reciprocal legislation. Actually, I think we already have it in the law that was passed last fall. And I think the administration could get even more aggressive on it. Right now, the Germans and the British are negotiating with the Japanese on the precise issue you just raised, and they are making great progress.

Senator CHAFEE. Well, I'm more interested in what we can do. We can do the same thing.

Mr. FREEMAN. Yes, we can do that. We have the law. I think if we enforce the law and have a strong GATT round coming up very quickly on services, including financial services, I think that's what our Government can do and be successful at it.

Senator CHAFEE. Thank you both for coming.

Mr. Thornton, did you come from San Francisco yourself?

Mr. THORNTON. Yes, I did.

Senator CHAFEE. Just for this?

Mr. THORNTON. Yes, I did.

Senator CHAFEE. Well, that was a long climb for a short slide, but we appreciate your making it.

Mr. THORNTON. Well, I'm honored to be able to make the contribution.

Senator CHAFEE. And you have made a contribution. Thank you very much.

[Whereupon, at 12:52 p.m., the hearing was concluded.]

[The following was received for the record:]

INGERSOLL

EDSON I. GAYLORD
CHAIRMAN OF THE BOARD
AND PRESIDENT

Senate Committee on Finance
Honorable Senator Packwood, Chairman
Trade Oversight Hearings

This statement is respectfully submitted to the Senate Committee on Finance. I was asked on short notice to testify at your Trade Oversight Hearing on Wednesday, November 20, 1985, and regret I was unable to change my schedule in order to appear.

I am Chairman of the Board of Ingersoll International, which has six wholly-owned subsidiary companies engaged in the design and manufacture of heavy, custom-built machine tools and various support services. Our company's headquarters are in Rockford, Illinois. Sixty percent of our activity is based in the United States; the other forty percent in West Germany. The market for our machines and services is international; some years as much as sixty percent of the machines we produce are shipped outside of the United States and West Germany, the two countries where we build machines.

Ingersoll is a private company and, therefore, our trading statistics are not public, but we are one of the largest machine tool companies in the world. We now employ approximately 3,700 people and our annual shipments exceed $200,000,000. We build some of the largest machines built any place in the world. Our customers are both high-production companies, such as automobile producers, and low-volume users, such as the builders of turbine generators for power stations.

We both sell to and compete with Japanese companies, as well as those from the other two prominent machine tool building countries, Germany and the United States.

The United States machine tool industry, a relatively small business segment, is nevertheless made up of a wide variety of companies; some, such as ourselves, supply a small number of specialty, big-ticket machining systems, and others produce rather large quantities of standard machines which are cataloged and distributed around the world.

THE INGERSOLL MILLING MACHINE COMPANY, ROCKFORD, ILLINOIS 61103 TEL. (815) 987-6000 TELEX 257427

All segments of the U.S. machine tool industry are under severe competitive pressure, and particularly the builders of standard machines, which is the market area in which the Japanese builders excel.

To the question--"Does the U.S. machine tool industry need protection?"--our answer is that the machine tool builders need to become once again internationally competitive, and this will not happen if they are protected from world competition.

Much has been said about the unfair practices of the competitors from Japan. How much unfairness there has been is not particularly important at this time because the complaints are, for the most part, leveled at actions from the past. There are no restrictions now against the sale of U.S. machines into Japan. The Japanese government is encouraging its industrial companies to look to the United States for certain of its machine tool needs.

And there is no evidence that the supply of machines into the U.S. from Japan is now subsidized. The claim that the Japanese dumped their machines in the U.S. in the past may have had some validity, but not now.

Much as been written about the role machine tools play in our defense capability. It is my opinion that this patriotic argument is a cover-up for a plea for protection from Japanese competition by those companies who are unable to compete internationally because they failed to invest in and otherwise prepare their companies for today's competition.

What the U.S. needs in order to defend itself are vigorous and internationally competitive industrial companies that can, if need be, out produce the rest of the world in whatever the military forces need, just as we did during World War II. We cannot be so capable if we are shielded from the competition.

What's needed is the managers, the people, the spirit, the technological competence, the ability to mass produce, the ability to move raw materials...and machine tools. Machine tools are a single element in the entire system. But, if protectionism is what's needed, you've got to take care of it all, the whole system. Take care of steel, of raw materials, of all the big companies. Protect them all.

What will machine tool builders do if they get this grace period? Will they all start investing in their companies? Will they all begin efforts to develop new products? There is no historical evidence that they will. Taking away competition does not spur people into action.

A virile machine tool industry is an important, although numerically small, part of our total industrial strength, but to protect it against world class competition just to keep it alive in the event of a crisis is overplaying its importance and fosters retaliation which will threaten our total industrial strength.

To protect the machine tool industry now from offshore competition would be a classic case of poor timing. Most of the damage to the industry from offshore competition has already occurred. The industry is in the process of reshaping itself to once again resume a position of international leadership.

The European machine tool industries, which grew without interruption from the ashes of World War II to their pre-war leadership role between 1950 - 1965, seemed to go into an eclipse during the late 1960's and 1970's. They too faced a real possibility of losing their international competitiveness. Most companies, like those in the U.S., lost their profitability.

They have responded in the first half of this decade by aggressive development, and it appears they are once again a leading competitor in the world market. In many areas, they have gone by the Japanese, as well as the U.S., in technology.

As this competitive race develops between Japan, Germany and the United States, the industry is changing shape; there are many new corporate link-ups between the relatively small companies building machines in all three countries.

To put up a protective wall around the U.S. machine tool builders would represent a damaging intrusion into this restructuring process.

There is every reason to believe that such protection would be very unsettling to the part of the industry that is competitive now.

Edson I. Gaylord
Chairman of the Board
The Ingersoll Milling Machine Company

November 18, 1985

CWT
CONSUMERS FOR
WORLD TRADE
1001 Connecticut Avenue, N.W.
Suite 800
Washington, D.C. 20036
202-785-4835

November 18, 1985

STATEMENT FOR THE SENATE FINANCE COMMITTEE

"U.S. Trade Policy"

Consumers for World Trade (CWT) is a national, non-profit membership organization established in 1978. CWT supports expanded foreign trade to help promote healthy economic growth; provide choices in the marketplace for consumers; and counteract inflationery price increases. CWT believes in the importance of increasing productivity through the efficient utilization of human and capital resources. CWT conducts its educational programs to keep American consumers informed of their stake in international trade policy and speakes out for the interests of consumers when trade policy is being formulated.

****

Directors
DOREEN L. BROWN
President, Consumers for World Trade
C. FRED BERGSTEN
Director, Institute for
International Economics
JOAN R. BRADEN
Senior Vice President, Gray & Co.
TIMOTHY L. ELDER
Washington Manager of
Governmental Affairs,
Caterpillar Tractor Company
JOHN R. FRAHM
Manager, Government Activities-International
Operations, 3M Corporation
ISAIAH FRANK
Professor of International Economics
Johns Hopkins University School of
Advanced International Studies
ROBERT N. HAMPTON
Consultant, Agricultural and
International Trade
J. M. COLTON HAND
Vice Chairman,
Committee of 100 on the Federal City
HENDRIK S. HOUTHAKKER
Professor of Economics, Harvard University
A. W. JESSUP
Washington Representative,
U.S. Council for International Business
FRED J. MARTIN, JR.
Vice President, Washington Representative,
Bank of America
ROBERT S. McNAMARA
Former President, The World Bank
GERALD O'BRIEN
Executive Vice President, American
Importers Association (retired)
WILLIAM MATSON ROTH
President, Roth Properties
SEYMOUR J. RUBIN
Executive Vice President, American Society
of International Law
PHILIP H. TREZISE
Senior Fellow, Brookings Institution
Executive Director
JANE E. DOCKERY

Fairness is certainly an important aspect of the international trade debate. What is missing in the discussion is the question of fairness to the consumer.

Read our trade laws and you will find almost no mention of the consumer's interest in trade. Listen to the clamor for protection and notice how little is said about the costs to be borne by the consumer.

This is not a situation peculiar to the United States. Every jurisdiction in the world, with the possible exception of Hong Kong, acts in the belief that when trade policy is being made the consumer and his concerns can safely be ignored.

Fair trade for the consumer is trade that maximizes his freedom of choice and the value he receives for his expenditures. In an ideal world, it would be considered an unfair act to restrict or impair his access to suppliers world-wide. In that kind of world the American consumer would not be asked to buy sugar at five times the world price in order to benefit 12,000 beet and cane farmers. In that kind of world, European and Japanese consumers would not have to pay inflated prices for cost-of-living items like bread or beef in order to underwrite agricultural policies that border on the irrational.

The unhappy fact is that everywhere consumers as consumers and consumers as taxpayers are victimized by political decisions to shelter industries from foreign competition and by governments which believe that the road to prosperity is paved with quotas on imports and subsidies to exports. If this pervasive unfairness could be reduced in scope and intensity, the plaintive cries for "level playing fields" in international trade would come remarkably closer to realization.

We hope that your committee will give full attention to the issue of fairness to the American consumer. Last year the Senate sent to conference a trade bill with the provision authored by Senator Chafee that would have required a consumer impact statement--essentially a cost-benefit analysis-- when protectionist laws or actions are being considered. It was intended to introduce the concept of fairness to the consumer into the debate, before deciding to burden his budget and to limit his freedom of choice. As might have been predicted, the provision was dropped by the conference. The idea should be revived and as soon as possible made part of our basic trade law.

Meanwhile, the best hope for consumers at home and abroad lies in the preservation and strengthening of a system that seeks to expand the area of international specialization and thereby to increase the total gains from trade. Many elements of such a system already are codified in the General Agreements on Tariffs and Trade. We need to broaden the GATT's coverage to clarify some of its rules. The overriding necessity, however, is for the big trading nations to live up to the commitments made in the General Agreements, commitments which they regularly swear to observe and which they regularly violate.

-- --

The GATT, for all its imperfections, provides a set of standards against which to judge what is fair and what is unfair in international trade policies. It is not fair, for example, to impose quotas on imports except in specifically limited circumstances. It is unfair to subsidize exports, again subject to limited exceptions. Read in any reasonable light, the GATT does not make provision for so-called voluntary export restraints, or like hyprocritical forms of protection against imports. The first article of the GATT tells us that it is unfair to restrict imports of textiles from South Korea or India and not from France or Canada.

All of these practices are unfair to the consumer-- in the case of export subsidies, to the consumer in his taxpaying manifestation. His interest, therefore, is in a GATT which is observed with greater exactitude, a GATT to which the principal Contracting Parties give steady and conscientious support, even when it appears to hurt.

It is certainly not a consumer interest to have each Contracting Party able to decide for itself what are the standards for fairness. If the United States is free to make that decision, so is the European Community, so is Japan, so is Canada. That is the path to anarchy in international trade. Your committee will do a signal service if it makes that single point as a result of these hearings.

WRITTEN TESTIMONY

Submitted to the

United States Senate Committee on Finance

in connection with

Oversight Hearings on

United States Trade Policy

November 19, 1985

My name is Ron Kahle. I am a pork producer from Kearney, Nebraska, and am President of the National Pork Producers Council (N.P.P.C.). I am submitting this testimony for the record on behalf of the 110,000 members of the National Pork Producers Council (N.P.P.C.), the largest commodity dues paying organization in the U.S.

The N.P.P.C. is particularily concerned about the treatment of agricultural commodity products under the U.S. trade laws. We are specifically speaking of situations where agricultural products produced abroad are subsidized or dumped in the United States or otherwise unfairly traded. Pork producers are supportive of fair and equitable trade, but in some agricultural sectors there is little or no competition because of subsidized or dumping of imports that prevent U.S. producers from being able to compete on an equal basis.

Under U.S. trade statutes, agricultural commodities have not been given the kind of relief industrial commodities receive. When looking at the track record of agricultural cases, the message is clear. The attached article, written by Commissioner Seeley Lodwick of the International Trade Commission (ITC), explains that of the 11 unfair trade injury investigations concerning agricultural products filed at the ITC over the last 3 1/2 years, only one case ended in an affirmative determination. This success rate of 9% compares with an approximate rate of 50% for cases concerning industrial products. The recent decision of the ITC in the countervailing duty investigation concerning imports of subsidized swine and pork from Canada, exemplifies the difficulties which producers of agricultural commodities have in obtaining relief from unfairly traded imports under the U.S. trade statutes.

The problem may be due to a lack of understanding of the basis upon which agricultural products are traded. Agricultural products are different from industrial products in the sense that most agricultural products must be treated or processed before they can be sold to end users or manufacturers. While they cannot be sold as is, they can be initially processed to yield a marketable good -- for example, slaughtering live hogs into fresh pork. That means pork producers and initial processors work together to produce a product and therefore are part of the same industry.

In addition, the impact of unfair trade practices in the agricultural sector differs from that found in the industrial sector. When the ITC has examined agricultural products it has applied the same test as with industrial products, looking for specific instances of price undercutting, for example, rather than examining the effect of supply on the price of commodities in the marketplace.

Agricultural markets function differently than industrial markets. In the agricultural sector, an increase in supply decreases the prices of our products. Take, for an example, pork which is a commodity just as swine is a commodity and both are traded on the commodities market. Pork prices fluctuate from day to day with changes in supply and demand, and they have a direct relation to the price of hogs. Increases in the supply of pork have negative effects on pork and hog prices.

Senate Bill 1629, introduced by Senator Grassley (R. Iowa) and supported by other senators on the Committee, addresses a necessary clarification of the Trade Act of 1930 to reflect the way imported products affect agricultural products. Senate Bill 1629 defines producers and initial processors of products linked by a single continuous line of production as part of the same industry. This allows pork producers, processors or both to file a petition preventing subsidized or dumping of imports. Since imports of the processed product affect all elements of the industry, it only makes sense to allow producers as well as processors to petition for relief. As it stands now, pork producers cannot bring a countervailing duty action against imports of fresh pork because producers are not considered part of that industry, even though imports of fresh pork certainly affect pork producers. Similarly, cattlemen could not bring a case against beef imports being dumped or subsidized because cattlemen would be considered producers of live cattle and not producers of the product. However, beef imports certainly affect cattlemen and cattle prices. Without this clarification of legislative intent reflected in S.1629, cattlemen would have no other recourse since live cattle are not imported into this country for human consumption. The same dilemma is applicable to all producers in the agricultural sector. Even though an import of an initially processed version of their product would have dire effects on their businesses, they may have no standing to complain. S.1629 applies to all raw agriculture products. The bill would clarify the intent of Congress with regard to the application of the countervailing and antidumping statutes to agricultural commodities.

On August 15, 1985, the Department of Commerce issued a countervailing duty order imposing duties on imports of Canadian live swine, but did not order the imposition of duties on Canadian pork. The consequence of the ITC decision is that

Canadian packers will now slaughter the live hogs into fresh, chilled or frozen pork before sending the product over the border, thereby eliminating much of the beneficial effect which the countervailing duties on swine would have on domestic producers and packers. With the raw and initially processed products so integrally related, duties on only one do little to help the domestic industry. In essence, the U.S. pork producers have won the battle but lost the war.

Indeed, the expected shift from hogs to pork has already begun. Imports of Canadian hogs are down over the volume of imports prior to the ITC's decision. On the other hand, Canadian statistics reveal a 10% increase in pork exports to the U.S. in August (the month in which duties on swine went into effect) over the average monthly export figure for January-July 1985. In September, Canadian pork exports to the U.S. rose even further to a level 20% higher than the average for the first seven months of this year.

The ITC's determination in the case of Canadian imports has come at the same time that pork imports from other countries are also increasing, particularly from the European Community ("EC"). Comparing imports from the EC for the first six months of 1984 and the first six months of 1985, USDA figures reveal that there has been a 156% increase in imports of fresh, chilled and frozen pork from EC producers and processors. These imports are, of course, also subsidized

0506M

under the EC's Common Agricultural Policy ("CAP"). With overall imports increasing dramatically, the ITC's pork decision was particularly untimely.

Congress stated in the legislative history of the Trade Agreements Act of 1979 that agricultural commodities require special attention with respect to the application of the injury provisions of the countervailing duty and antidumping statute.[1/] Special concern was expressed in the case, for example of raw and initially processed products, particularly in the case of livestock. In applying this legislative intent in past cases, the ITC developed a two part test to determine whether raw and processed agricultural commodities are like products.[2/] If so, producers of the

---

[1/] Senate Finance Committee Report on the Trade Agreements Act of 1979:

> "Because of the special nature of agriculture, . . . special problems exist in determining whether an agricultural industry is materially injured."

The report went on to imply that there was a special relationship, for example, between cattle farmers and processors. S. Rept. No. 96-249, 96th Cong., 1st Sess. 88 (1979).

[2/] See Lamb Meat From New Zealand, Inv. No. 701-TA-80 (Preliminary), USITC Pub. No. 1191 [3 ITRD 1725] (1981); Frozen Concentrated Orange Juice From Brazil, Inc. No. 701-TA-184 (Final), USITC Pub. No. 1406 [4 ITRD 1693] (1983); Fish, Fresh, Chilled or Frozen, Whether or Not Whole, But Not Otherwise Prepared or Preserved From Canada, Inv. No. 701-TA-40 (Final), USITC Pub. No. 1066 [2 ITRD 53-1] (1980).

raw commodity are deemed to be members of the same industry as the processors and can seek relief under the trade statutes against imports of the processed product.

Unfortunately, the ITC, has focused increasingly on legal relationships within an industry and has ignored economic relationships between the commodity producers and processors. In the pork industry, although both pork producers and packers share a significant commonality of economic interest resulting from the nature of the pork market, the second prong of the ITC's legal test was not satisfied because only 4-5% of pork producers actually own packing plants. Nonetheless, it is very clear to individuals familiar with pork and other agricultural commodities, that the economic interdependence of producers and processors and the impact of imports upon them is the same regardless of whether 5% or 90% of the processing plants are owned by producers. In the ITC's decision to impose a requirement of such legal relationships is both inappropriate and irrelevant. This view was supported in a dissenting opinion of ITC Vice Chairman Liebeler, one of three Commissioners voting in the case.3/

Realistically, the Commission should have focused on economic relationships in examining the injurious impact of

---

3/ Live Swine and Pork from Canada, Inv. No. 701-TA-224 (Final), USITC Pub. No. 1733 (1985).

subsidized or dumped imports on agricultural commodities. Moreover, where the processed product is produced from the raw commodity substantially or wholly through a single continuous line of production, that fact in and of itself demonstrates sufficient commonality of economic interest to satisfy the like product test. Pork producers have a firm opinion on this point, since it is difficult to conceive of any other commodity which better satisfies the single continuous line of production test.

S.1629 provides that producers and processors of agricultural commodities shall be considered members of the same industry if they meet either of two tests articulated in the bill. If the raw product and the processed product are wholly or substantially linked through a single continuous line of producton, then such raw and processed products are deemed to be like products and the producers and processors of the products are deemed to be members of the same industry. If producers and processors can demonstrate sufficient commonality of economic interest, which will likely include a showing of some degree of a single continuous line of production relationship, they can also be considered members of the same industry. Evidence of legal relationships may be considered, but the bill emphasizes that the key relationships are economic, whether they be imposed contractually or by the nature of the market.

This legislation would require the ITC to apply the injury provisions of the countervailing and antidumping statute to agricultural commodities in a manner which reflects the realities of the way such commodities are produced, priced and sold and by the way the producers and processors are affected by unfairly traded imports. In the case of pork, this legislation would have increased the chances that the ITC would have found that Canadian imports were causing injury to the entire industry, including packers. The impact of imports of both swine and pork would have been properly combined so that the actual and total impact of Canadian imports would have been taken into consideration by the ITC.

In addition, the bill would insure that producers of raw commodities have standing to file petitions for relief under these statutes against subsidized or dumped imports of the processed commodity. As an example, beef producers could bring cases against unfairly traded beef imports causing injury to the producers. Since the live animal is generally not imported (pork is an exception), livestock producers would be precluded from bringing cases against meat imports, unless their industries happened to be sufficiently vertically integrated under the ITC's present policy. There is great support for the bill. For example, at the hearings before two House Agriculture subcommittees on the House companion bill, H.R. 3328, representatives from the American Farm Bureau, the National Pork Producers Council and the lamb and raspberry industries testified in favor of the legislation. The National Cattlemen's Association also supports this legislation. S.1629 is crucial to protect the agricultural sector from unfairly traded products.

We appreciate the opportunity to submit this testimony on behalf of the National Pork Producer Council.

OVERSIGHT HEARINGS ON U.S. TRADE POLICY

THURSDAY, NOVEMBER 21, 1985

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The committee met, pursuant to notice, at 9:30 a.m. in room 215, Dirksen Senate Office Building, Hon. Bob Packwood (chairman) presiding.

Present: Senators Packwood, Chafee, Wallop, Long, Bentsen, Moynihan, Baucus, Boren, and Bradley.

The CHAIRMAN. The hearing will come to order, please.

We are pleased to have Congressman Ralph Regula as our first witness, and he has to get back to the House because they are marking up the continuing resolution.

There are those of us, Congressman, who wouldn't mind delaying you from going back to marking that up; but I think, under the circumstances, we had better get started. I appreciate you coming over. Go right ahead.

STATEMENT OF THE HONORABLE RALPH REGULA, U.S. HOUSE OF REPRESENTATIVES, STATE OF OHIO

Congressman REGULA. Thank you, Mr. Chairman. I appreciate the opportunity to testify early, and I certainly commend your committee for taking on the task on trade. I noticed in this morning's paper that you have a massive trade package coming, and it is something of great concern. I would say second only to the deficit in terms of importance, in the 16th District, is the matter of trade.

I would like to limit my testimony to revisions that I believe are necessary to section 201 of the Trade Act of 1974, particularly as they affect filings by the steel industry.

As vice chairman of the congressional steel caucus in the House, the difficulties the steel companies have encountered under section 201 filings have long been a concern. And I might say it applies to all of the other industries that have a similar type of problem.

I am certain that everyone here is well aware of the enormous burden placed on the steel industry in recent years, due in part to massive growth in imports. While the voluntary restraint programs are showing some positive relief, further assistance is needed in order to revitalize American steel production, and I might add to make it a fair environment.

Certainly, the supervalued dollar has caused many of the problems for the industry as it faces steel imports. I would like to focus, however, on specific changes that can and should be made to section 201 to more fairly and appropriately evaluate and fashion remedies for 201 filings.

First, I think the injury standard needs revision. As you know, current law requires a finding that imports are a substantial cause of the industry's injury before section 201 relief is triggered. This mandates the initial conclusion that imports are not less significant than any other cause for the industry harmed. Therefore, if a more significant cause is found, relief is not available under 201.

There is no reason why the United States law should have a more stringent injury standard than what GATT requires, particularly in light of the massive import problem. Article XIX of GATT's "escape clause" requires only that the imports in question, and I quote directly from the GATT Agreement, "cause or threaten serious injury to domestic producers." Consistent with GATT, I strongly agree with many others who have proposed lowering the section 201 causation standard by requiring only a finding that imports are a "cause" of injury.

Second, the time required for resolution of a 201 petition frequently works to the extreme detriment of affected U.S. industries. During the months of 201 review, the imports in question continue to flow into the United States. This not only intensifies the harm to the United States industry but makes retroactive relief impossible.

I would propose as an interim relief that, upon filing of a 201 petition, liquidation of these imports be suspended. This would mean that entries of the final processing of the import paperwork would not be liquidated until the section 201 complaint was resolved.

This immediate remedy does not unfairly stop import flow, but rather leaves open the option of retroactive relief, such as applying tariffs back to the point of a 201 filing. Further, the uncertainty of suspension of liquidation makes it difficult for foreign countries to take advantage of the time required to resolve a 201 complaint, as "dumping" during the time of suspension would cease to be profitable.

Thus, this interim action would preserve retroactive relief while eliminating our trading partners' all too frequent practice of using the 201 time period to flood our markets, thus mitigating their losses when the 201 remedy is imposed.

Third, in order to affect objective relief, the 201 process must be depoliticized. Presently, the President has the authority to grant relief under section 201. While I do not advocate eliminating his role, I do believe that this authority more appropriately lies with the U.S. Trade Representative or the Secretary of Commerce.

This would solve several problems. The present system provides a formal forum for inter-agency disagreements over trade policy. With the President responsible for the decision to grant relief, the various Departments, such as State and Treasury, insert their parochial interests into the process. This clouds the issue and makes appropriate relief for the immediate 201 complaint remote.

With the authority placed with the USTR or Commerce, this arena is changed and the focus is shifted. While there will certainly remain many voices in the process, it will be more directed to the immediate concerns of the affected industry.

I believe that the President should maintain veto power over the recommendations of the USTR but that his veto should carry an alternative to the relief sought. Further, I feel that various proposals for relief should be presented to the President so that he, in exercising his veto authority, does not have a take-it-or-leave-it option.

Finally, the narrow definition of industry which is appropriate in unfair trade statutes is not appropriate in section 201 complaints. This problem was illustrated when the American steel industry recently applied for section 201 relief. The ITC divided the steel industry into a half-dozen or more segments and evaluated each separately in determining its recommended remedies. Thus, affirmative injury rulings attached to some but not to others. Only 70 percent were accorded relief.

Under the broad purposes of section 201, such narrow definitions of industry do not adequately and efficiently address the problem. Therefore, I would propose that the ITC be encouraged by statute to consider a broader definition of industry and not view as definitional precedent the narrower industry definition used in the unfair trade statutes.

I would like to add that Huffy Bicycle Co. in Ohio has expressed considerable interest in this hearing and my testimony. They have experienced an import increase from 17 percent in 1979 to 58 percent of the American bicycle market as of September 1985.

Huffy, along with many nonsteel companies across this Nation, would benefit greatly from the changes I have suggested to section 201, as they have encountered the same difficulties in seeking import relief, and I might add fairness.

I certainly applaud the committee's efforts toward rectifying these problems for our domestic industries, and I appreciate this opportunity to testify this morning.

The CHAIRMAN. Congressman, let me ask you this, very quickly: Over and over we are getting testimony from companies whose complaint is about the wage differential, which at the moment is not counted as an unfair trade practice in international competition. Should we define it as such and simply say we have reached the place where there areas we cannot compete with that wage differential, and we are going to give the companies temporary or maybe permanent protection?

Congressman REGULA. Well, I suppose that is what the VRA's do in the steel industry, is to provide in effect a 5-year period to offset the wage differential with technology. And I think perhaps that should be of a temporary nature, but I'm sure that for the long term you can adopt that type of policy if you are going to have a free world marketplace.

But I do think we need a period of time to do catch-up, because in the case of Japan, for example, that have taken the capital that they don't spend on defense and put it into technology—R&D and a lot of things that have given them a substantial advantage. We need to do the same thing in this country.

The CHAIRMAN. Let me give you a comparative example.

A textile industry has testified that they have modernized, their productivity has gone up, they cannot invest capital any faster.

And indeed, if you go through some of the textile mills of this country, they are sensationally modern.

Congressman REGULA. That is true.

The CHAIRMAN. They still say they cannot compete against the low wage rate differential. What do we do then?

Congressman REGULA. Well, I suppose what you are really asking me is, should wage differential be considered an element in determining whether there is dumping?

The CHAIRMAN. Not dumping so much, because that has a connotation of selling something even below the cost in your country—the other country's manufacturer.

Congressman REGULA. Well, that is true. Yes.

The CHAIRMAN. And in most of the wage differential cases there is not often an allegation of selling goods in this country at a cheaper price than the cost to manufacture in the foreign country; it is just that the cost to manufacture is so cheap that the domestic company can't compete.

Congressman REGULA. I think, as a pragmatic answer, The Chairman, there would have to be some measure of relief that is in the form of tariffs and/or quotas. That might be the only answer in industries where you are competing. And I don't think in the textile industry that the wage level is high as compared to the industrial base of this country. But, when you have $8 an hour versus 10 cents an hour, as it might be in some of the Asian countries, in a sense that is part of an unfair practice. What we need to do is push them to raise their standard of living so that you have some degree of comparability, and I don't know any other way to approach that than through tariffs and/or quotas.

The CHAIRMAN. Senator Baucus?

Senator BAUCUS. No questions, Mr. Chairman.

The CHAIRMAN. Congressman, I have no others. Thank you very much for taking the time to come this morning.

Congressman REGULA. Thank you.

The CHAIRMAN. All right, we will move on to a panel. We are going to skip around, because our second panel is not here. We will have R. Allan Leedy, representing Tektronix, and Charles Davis, my old friend Charley Davis, representing Electro Scientific Industries. I know they are both here, because I met with them earlier.

Then, after they are done, we will move back to Professor Jackson, if he has arrived, and the panel of Mr. Hufbauer, Mr. Lawrence, and Mr. Aho.

In introducing these two gentlemen, I might say I am very, very familiar with their companies; they are both located in Portland or suburban Portland, and they are both not only able to adequately compete against foreign competition in the United States but both of them are heavily involved in competition overseas, and the bulk of their employment is in this country, the bulk of their investment is in this country, and even with our wage structure they manage to compete somehow in most of the rest of the world.

Mr. Leedy, do you want to go first?

STATEMENT OF R. ALLAN LEEDY, JR., VICE PRESIDENT, SECRETARY, AND GENERAL COUNSEL, TEKTRONIX, INC., BEAVERTON, OR

Mr. LEEDY. Thank you, Mr. Chairman.

The CHAIRMAN. I might say that your testimony in its entirety will be in the record, and we would appreciate it if you could abbreviate it.

Mr. LEEDY. Thank you.

Mr. Chairman, I am vice president, secretary, and general counsel of Tektronix. And as you know, Tektronix is a leading manufacturer of test and measurement equipment and computer-related equipment in the State of Oregon. We have approximately $1.5 billion in annual sales and approximately 20,000 employees, most of whom are in Oregon.

I am privileged to be here this morning to testify. My remarks are going to be directed principally to the second of the questions raised by these hearings; that is, the question of whether or not a U.S. industry can compete with fair trade in world markets.

I think that there are probably three aspects of my written submission that merit some special emphasis.

First of all, I would like to say that my company is convinced that in our industry we can effectively compete on the basis of fair trade in the markets that we serve around the world, and that we are aggressively investing and spending on research and development of new products and on new manufacturing technologies to improve our productivity, in order to be able to meet the competition that we face from a variety of countries, including Japan, other countries in Asia, and countries in Europe.

As indicated in my written submission, we have in the past year spent some $188 million on research and development for new products. That represents this year more than 13 percent of our net sales, and it is an increase from under 10 percent only a few short years ago.

In addition, we have spent rather large amounts in investment in modern and sophisticated manufacturing techniques, with very good effect in improving our ability to utilize inventory and improving the ratio of cost of sales of our goods to the selling price.

The second point that I would like to make is that these efforts that we and other companies undertake in our industry can be more effective and more productive if they can be undertaken in a climate which is stable and which fosters the kind of national competitiveness that we seek to achieve.

There are numerous examples that I have stated, of tax policy, of export control policy, on which I think my colleague Charley Davis is going to talk in some detail, and other areas of Government regulation that bear on this issue. I would like to give, though, just one example that relates to company's experience that I think illustrates the point quite well.

For some time now, Tektronix has been seeking a director candidate who might be able to expand the company's experience and expertise in the area of manufacturing. In canvassing for available candidates to serve on our board of directors, we have found that nearly everyone who possesses the credentials for expanding in this direction would be barred from serving on our company's board of directors under section 8 of the Clayton Act.

As I believe you know, section 8 prohibits directors of competing companies, prohibits an individual, from serving on the board of directors of two companies that compete with each other. And the courts and the administration have interpreted this prohibition to apply to any kind of competition regardless of how significant it is in the overall sense. So, for example, companies as diverse as General Motors and General Electric might be seen to compete with some small piece of Tektronix in some small piece of their own business; and thus, the interlocking directorship would be prohibited.

In my view, this represents an absence of looking at the big picture, and I am going to be supporting legislation to amend and liberalize this rule.

Finally, Mr. Chairman, I would like to say that whatever the Government and the Congress does to create a more stable environment to give more priority to national competitiveness, perhaps the single most important issue now is the burden of the overvalued dollar that our products carry in overseas markets. And I would join those who urge the Congress to address promptly and effectively the task of reducing the size and reducing the cost of our Federal Government so that we can enjoy the fruits of our own efforts and the Government's efforts, working in partnership to make us all more competitive.

Thank you very much, indeed, for this opportunity to speak on what I think is today's most important issue.

The CHAIRMAN. Mr. Leedy, thank you. Now I would ask Charley Davis, who is an old, old friend of mine—you can tell the age difference; Mr. Leedy's father is an old friend of mine, and Charley Davis personally is an old friend. So, I guess, Charley, I fit into your generation.

[Mr. Leedy's written testimony follows:]

Statement of R. Allan Leedy, Jr.
Vice President, Secretary, and General Counsel
TEKTRONIX, INC.

Before the Committee on Finance, United States Senate
Washington, D.C.
November 21, 1985

Mr. Chairman and Members of the Committee. These hearings on how the United States, and U.S. companies, can respond to both fair and unfair trading practices in international markets are most timely, and Tektronix, Inc. appreciates this opportunity to testify. I am R. Allan Leedy, Jr., vice president and general counsel of Tektronix. As you know, Mr. Chairman, Tektronix is a leading manufacturer of electronic test and measurement instruments, graphics terminals and design tools, and communications equipment with annual sales of about $1.5 billion and 20,000 employees world-wide -- most of them in the State of Oregon.

Tektronix' market is a global one. Sales outside the United States totaled $514 million in 1985, representing 36 per cent of our annual sales and supporting more than 7,000 jobs at Tektronix. We have a jointly owned manufacturing and sales company in Japan, and manufacturing operations in Britain, the Netherlands and the Channel Islands. We have our own sales and service operations in 20 countries, and local distributors in many others. In this global market we face stiff, direct competition not only from several major U.S. firms, but from Japanese, French, German, and Dutch companies. While our international market share varies from product to product and country to country, we have achieved and maintained a significant share of both foreign and domestic markets. Japan, for example, is our largest and fastest growing foreign market. We have had a dominant presence in Japan for 20 years because we have made a long-term commitment to serve that market.

My testimony will concentrate on Tektronix' approach to this foreign competition -- responding particularly to the second question posed by the Committee in its announcement of these hearings: "Can the United States compete with 'fair' trade."

Mr. Chairman, Tektronix is confident that we can continue to compete effectively, as we have in the past. But to do so requires increasing the efficiency and productivity of our current manufacturing operations. It requires increased levels of investment. It also requires more sophisticated strategic planning based upon world market conditions, not just domestic ones. We are taking major steps in all these areas.

Improved Efficiency

To increase the efficiency of our current operations, we have implemented "manufacturing resource planning" (MRP) in most of our facilities at a cost of more than $50-million over the past four years. MRP is a computer-aided system of resource planning and cost control. We have 19 plants certified with "MRP-Class A" ratings as determined by independent auditors. That is more top-rated manufacturing capability than anyone in our industry. We also have the largest manufacturing organization ever certified with this high rating. More important, our productivity has increased from $44,000 per employee in 1981 to $70,000 this year. With MRP and other measures, such as "just-in-time" (JIT) component scheduling, we are now able to turn around our inventories six times a year, compared to about 3.6 times just a few years ago.

Investment

Difficult as it is with current profits generally down in our industry, we are investing heavily in our operations, mostly in the United States. We are investing in research and development that will result in the innovative products we need to remain competitive in the fast-moving electronics industry. And, we are investing in people -- the human knowledge and skills so crucial to competing successfully.

In 1985 we invested $188 million in corporate R&D. That was 13.3 per cent of annual sales, compared to less than 9 per cent devoted to R&D in 1981. As a result, we're introducing new products faster than ever at both higher technology levels, where new markets are to be found, and at lower technology levels, where we face the greatest challenge to our existing markets, particularly from Japan. Our newest products include a sophisticated portable digital oscilloscope, an advanced new fiber optic measuring device called a "dual wavelength time domain reflectometer," and a very low cost portable oscilloscope.

Our employees in academic year 1984/85 were reimbursed more than $9.3 million in tuition costs for educational programs. A full 6,626 course enrollments were conducted on our own campus. Some 89 current Tektronix employees serve continually as adjunct advanced engineering faculty at 9 local area schools to help meet the present acute shortage of faculty (while undergraduate enrollment nationally has more than doubled in the past decade, faculty have increased only 20 per cent; in Oregon, about 45 per cent of qualified electrical engineering student applicants have to be turned away due mostly to lack of faculty).

Global Market Strategy

Tektronix has an extensive international marketing strategy, and we are working constantly to refine and strengthen it. It is based on three major commitments:

-- to meet the competition head-on with new products

-- to expand overseas sales operations and improve the effectiveness of existing ones

-- to develop strong, defensible positions in new markets

The increasing productivity and new products discussed earlier are the keystone of our global market strategy. To improve our sales in Europe, we have invested in recent years in marketing, sales and service organizations. We also have restructured our European operations for greater marketing flexibility and local control. A special marketing team has been dedicated to developing business in the People's Republic of China -- a major new market. Last year we opened a cooperative service facility in Beijing, and assembly in China of some portable instruments will commence soon.

It should be clear to the Committee from these few examples, Mr. Chairman, that we are not waiting or depending upon government actions to make us more competitive in world markets. We are taking the initiative ourselves, and we are doing so by committing our own resources "up front." There can be no question, however, that our efforts will be more successful in a stable and supportive government policy climate. I would like, therefore, to offer the Committee several policy suggestions that Tektronix believes would contribute to the international competitiveness of U.S. companies:

Competitive Tax System

Taxes are a major factor in the international trade equation, and changes in our tax system should be designed to put American companies on as equal as possible a footing with our foreign competitors. Unlike most foreign tax systems, ours is biased against savings and investment, thus raising the cost of the capital that is crucial to competing in world trade. Treatment of earnings abroad under Subpart F ignores the tax policies of our competitors, and falsely assumes we operate abroad to avoid U.S. taxation. Our heavy emphasis on taxation of income, which so directly constrains investment, puts us at a distinct disadvantage with most of our competitors who tax consumption as well. If Japan installs a value-added tax, the United States will be left as the only major industrial nation depending essentially on income taxes. To make our tax system more consistent with those of our competitors, we need to give serious consideration to establishing an export-rebatable consumption tax with reduced rates of corporate income tax.

R&D Incentives

Tektronix believes strongly, based on its own experience, that investment in research and development is investment in tomorrow's competitive products and services. The investment tax credit wisely enacted by Congress in 1981 has paid handsome dividends in preserving American competitiveness in advanced technology industries. Without the rather significant trade surplus the electronics industry maintained until just last year, our massive trade deficit would be even worse. We should retain an R&D tax credit, and expand it to cover company investments in university basic research.

Regulation and Operating Flexibility

To compete effectively in international markets, American companies must have as much operational flexibility as possible -- at least as much as our foreign competitors. Yet, in fact, few of our competitors face the degree of regulatory constraints that American companies continue to encounter. Let me give two examples: export controls and anti-trust.

Despite recent Congressional changes in the Export Administration Act which have removed, or promise to remove, national security export controls on some products, the United States continues to encumber exporters of high technology goods with extensive national security restrictions. The licensing process remains complex and difficult to administer, resulting in significant loss of business from delays as well as license denials. The national security and foreign policy benefits of these controls are questionable, at best. Our competitive position would be significantly improved by narrowing the controls to items with significant and direct military applications, and by eliminating the many remaining controls that are unilaterally imposed by the United States despite the availability of similar items from foreign sources.

As simple a matter as finding qualified appointees to Corporate Boards of Directors is made unnecessarily difficult by U.S. anti-trust law. Section 8 of the Clayton Act prohibits a person from being a director in two or more corporations which are competitors. With today's larger, more diversified corporations, this prohibition has become a major constraint both on corporations in need of knowledgeable outside directors, and upon the personal freedom in the market place of corporate directors. Since the Clayton Act became law, most of the abuses of interlocking directors have been addressed and precluded by separate financial securities laws.

Yet the Federal Courts and regulatory agencies have continued to take the position that any degree of competition between two companies, no matter how slight, precludes a director of one being appointed a director of the other. They have failed to recognize competitive realities. Those realities require at least a de minimis standard which would permit appointment of outside directors among companies who compete only minimally with each other. The cost to American companies in compliance efforts and lost talent is a cost not generally incurred by our foreign competitors, and it is just one of hundreds.

In his most recent book, Comeback, Ezra Vogel concludes that the United States does have a competitive policy. "That policy," he says, "is to give competitiveness lower priority than security and regulatory policy." We need to reverse those priorities and impose rules of reason upon our regulatory systems. Only that way will U.S. firms have the flexibility to respond effectively to competitive challenges.

Stable and Open Global Economy

A stable and more realistic valuation of the U.S. dollar in relation to foreign currencies is the single most important immediate step the U.S. government could take to enhance U.S. competitiveness. That, in turn, requires significant reduction of the federal deficit. I realize, of course, that this Committee is currently in conference with the House on deficit reduction legislation. I can only express the hope that the effort will be successful. If it is not, or if it is significantly delayed, it may be necessary to reconvene the Bretton Woods Conference to attempt to modify the present free-floating currency system to eliminate distortions like the one that has plagued the dollar for the past several years. If U.S. federal deficit reduction is difficult to achieve, a new currency arrangement will be even more so. We simply must effectively confront and reverse our own deficit, and we must do it now.

Finally, Mr. Chairman, a new round of global trade negotiations would serve the goal of increased U.S. competitiveness. By emphasizing, as I have in this testimony, the view that American companies can compete, I do not mean to imply that "unfair" practices do not exist, or that there is not urgent need to strengthen the rules of international trade, both under the GATT and through bilateral agreements wherever we can achieve them. The Congress should authorize the President to enter into new global negotiations as soon as possible. That authority should, in the view of Tektronix, include authority to further reduce U.S. tariffs on a reciprocal basis, as well as enter into agreements on various non-tariff barriers.

Strengthened protection of intellectual property should be one of the top priorities in those negotiations. Maintaining and improving our competitive position depends heavily upon our ability to protect the innovations we are paying so dearly to develop. The competitive damage from foreign violation of proprietary intellectual property rights will become even more severe as we and other electronics companies become increasingly involved in producing software products, with respect to which the international proprietary rules and compliance are particularly weak. The "reciprocity" approach adopted by Congress in the Semiconductor Chip Protection Act of 1984 is an appropriate way of inducing foreign cooperation, and that approach should be followed in other aspects of intellectual property protection. In addition, it would make sense to eliminate the injury standard for patent and copyright violations under Section 337 of the Trade Act of 1974.

Mr. Chairman, our business was founded on principles of dedication to customer satisfaction, technological innovation, productivity and people. Those principles remain sound ones as we face unprecedented foreign competition. To meet that challenge, we are investing -- and will continue to invest -- primarily here in our own country and in our own people. We ask only that the Federal government provide us the freedom of action we need to respond effectively.

Thank you for this opportunity to share our views on what is clearly the most challenging issue of our day.

STATEMENT OF CHARLES DAVIS, CORPORATE SECRETARY, ELECTRO SCIENTIFIC INDUSTRIES, INC., PORTLAND, OR

Mr. DAVIS. Thank you, Senator, and Senator Baucus.

I am the corporate secretary for Electro Scientific Industries, as Bob mentioned, a company in Portland, OR. We have been in business for 32 years. We are a relatively small company. We do about $85 million business a year, with $1,000 employees throughout the world. We supply state-of-the-art equipment to the microelectronics industry throughout the world, and in answer to the question: Can the United States compete with fair trade? Our answer is a confident "Yes." That is a "Yes" that is based on the expectation that regulation of our business will also move to state of the art.

We know that each year we have to do better than we did the year before in terms of the technology we design and the products we manufacture and sell. We know that the competitive forces throughout the world are just behind us all the time. And with respect to the export control to the U.S. Government, we ask that they be as competitive as the export controls in other parts of the world. In short, we and our Government have to be as efficient in providing the customer with a satisfactory product as XYZ Co. in Japan and its Government, or ABC Co. in Sweden and its Government, in terms of the effect of controls, in supplying a product to its customers throughout the world.

One of those serious problems we face is the problem of delay in export regulation. We feel that none of our products are so unique and none of our secrets are so really secret that we should be having to be under export control at all. But, so long as we are, we think the Export Administration should perform at a very efficient and responsible level. That has not always been the case; it isn't the case today.

Two of our executives have just returned from China, where they saw state-of-the-art products of about 10 years ago that we are not allowed to sell in China. These products were developed by the Chinese themselves, who would have preferred to buy a better product that we have here, and they would have bought it from us had it been possible for us to export it to them. Instead, they do it with what looks like a 15-year-old washing machine, although it is a piece of equipment that will do exactly the same thing as this one will do; but ours will do it faster, enable them to make a lot more television sets a lot more quickly. And we favor that kind of opportunity for us to be involved in.

On another level, the state of the art in the semiconductor industry is illustrated in the reports of the Institute on Semiconductors in China, which says throughout that they know as much about the theory of the semiconductor industry as we do, but that technology we cannot move in and out as we can in Western countries.

We will be asking and pressing for an earlier decision about the opportunity to ship products that qualify as being available in quantity in foreign markets in order to compete in the Chinese market.

The difficulty here is that the regulations proposed will not be adopted until some time next March or April by OEA, and after that it will take them time to make a decision. But this competitive market in China is developing right now, and we have to, next week, decide what we are going to do about it.

So we would ask that, without proposing anything that the Congress really doesn't know, I guess, that Government has to operate more efficiently and more effectively in its control role, and we suspect that might be helped if the police mentality of the regulators were altered to see that part of their responsibility is to encourage international trade, encourage the movement into this world economy by U.S. companies, and to limit the amount of police action they see themselves as doing.

I appreciate being here. If I can respond to questions, I will be happy to do so.

[Mr. Davis' written testimony follows:]

Electro Scientific Industries, Inc.
13900 NW Science Park Drive
Portland, Oregon 97229
(503) 641-4141 • Telex 474-2064

TESTIMONY OF

Charles Davis, Corporate Secretary

Electro Scientific Industries, Inc.

Portland, Oregon

Before the Committee on
Finance of the U.S.
Senate
November 21, 1985
Washington, D.C.

My name is Charles Davis. I am Corporate Secretary of Electro Scientific Industries, Inc., Portland, Oregon.

Our testimony does not speak to the over-valued dollar or the need for a revision of the U.S. tax code. It is about export controls and the administration of those controls which unnecessarily adds to the cost of our products and jeopardizes our competitive position in Europe and the Pacific Rim. We argue that the fair trade challenge is for the United States government to interfere with the conduct of business by our private enterprise companies only as much as is clearly necessary to protect the national interest.

Electro Scientific Industries, ESI, is a major supplier of equipment to the microelectronics industry. We design, manufacture and market products that help customers reduce production costs, increase yields and improve product quality.

We are a pioneer in the use of lasers in electronics. ESI is the world leader in laser processing of microelectronic circuitry. Our lasers perform a wide range of tasks for semiconductor and hybrid circuit manufacturers.

We are also a leading manufacturer of equipment used to produce, handle and measure chip capacitors and resistors--important component parts used in modern electronics.

We produce high precision instruments sold around the world to calibration and electrical standards laboratories.

Headquartered in Portland, Oregon, ESI has principal production facilities in Oregon and California. The Company employs about 1,000 people and operates sales and service offices worldwide.

We have had a lot of experience with regulatory agencies of the United States government, the State of Oregon and foreign governments as well. Our company includes wholly-owned subsidiaries in Japan, Hong Kong, West Germany, France, Italy, The Netherlands and the United Kingdom, where we have learned about the law and controls on business practices. Management and independent audits of our performance assure strict compliance with the laws and regulations wherever we operate, including those occasions where the laws are clearly unreasonable and ignored by others. That is, when others, including competitors, short-cut compliance with the advice that it is "local custom" to do so. We even pay our parking tickets in Paris. To us, full compliance with the laws and regulations is part of our way of doing business.

We started our business in 1953 and now have annual sales of about $84,000,000, nearly one-half of which are to customers in Europe or the Pacific Rim countries. Our annual U.S. payroll is about $20,000,000 and we have salaries of another $5,000,000 for our foreign subsidiaries.

We are an Oregon company, we are a United States company, operating in the competitive world economy. Our partner in this venture is the United States government. Mostly that is a silent partner, allowing us to take the risks and do the work, then sharing in the rewards. But, sometimes that partner is a burden that jeopardizes our ability to perform. We do not ask much of government, in our operations nationally or internationally, mostly just to be left alone. And, when government participation, regulation or surveillance is required, we ask that it be done with concern for the national interest and with recognition that we do operate in a world economy, a competitive world economy.

Our customers throughout the world expect us to provide a state-of-the-art product at a competitive price, when they need it and with reliable training and service support they can count on. If our product is not up to standard or delivery is delayed because of design or manufacturing errors, we can expect them to find another supplier. If we are delayed in delivery of a product because we cannot obtain an export license in time, our customer will look for a supplier whose government can move more quickly.

Export regulation is one of our most serious problems in meeting the challenge of 'fair' trade. On a recent visit to the Peoples Republic of China two officers of our company were shown many pieces of semiconductor equipment, primarily from Sweden - equipment we are not allowed to export. The Chinese commented that it was U.S. suppliers who were losing because they would be able to purchase the equipment elsewhere or build it themselves. They would prefer to buy U.S. made equipment but could do their work on equipment from other countries.

It appears that U.S. strategy of blocking the export of "Western" technology works not to our benefit but to that of Sweden and other countries. Markets that are off-limits to us are markets that encourage our competitors, enabling them to develop the technology and build the enterprises that may destroy us even in our U.S. markets, as well as in foreign markets where we are allowed to operate. Moreover, an organization in China that builds its own equipment because we cannot supply it for them is a potential competitor for us here at home and in the rest of the world.

If we are to regard participation in the international economy as more than "throw away" business, our company and our government must be competitive throughout the world. Our company and our government must understand down deep that a customer in the world economy is king of that economy. There are others who will serve that customer if we are unwilling or unable to do so. Of course, serving that customer includes making certain he likes the way he was treated by us and by our government. Buying a U.S. made product in the world economy may have been a privilege at some time in the past but it is no longer.

If we were designing a joint-venture between our company and the U.S. government to compete in the world economy - and to prevail in that competition - I doubt we would adopt the adversarial system now in place. Surely we would want firm control of technology to retain real secrets from those who would mis-use it. Just as surely, we would want those controls to be clearly understood and efficiently enforced with a minimum impact of the free flow of legitimate trade. I suspect we would want to minimize the police image of our export control because we would want to maximize our understanding and our cooperation together, each assuming good faith performance by the other. Somewhere in the operation of our joint-venture we would ask not only, "How many products have we kept from the Eastern bloc," but "How have we advanced our technology and our ability to compete in the world economy - compete against our political friends as well as against our political enemies?" Enforcement of export controls needs to be judged by the efficiency with which it achieves our goal - better performance of U.S. companies in the world market, as well as our shared goal of preventing the flow of products and technology to our enemies. An export license denied or a distribution license canceled is not the standard by which performance of the Export Administration Agency should be valued.

Our request of government:

1. Regulate to control only the products and technology that must be controlled and can be controlled to protect our national interest.

2. Place maximum reliance on Cocom and other international control agreements in the administration of regulations, duplicating those arrangements only where absolutely necessary.

3. Under all circumstances resolve disagreements between the several interested agencies of government before adopting control regulations and communicate that information in clear terms to exporters.

4. Provide a regulatory staff and facilities at all levels that can meet peak load responsibilities for the efficient performance of the minimum regulatory role.

ADM1D-47

The CHAIRMAN. I have some questions for both of you.

Mr. Leedy, you have a most perceptive statement on page 5, when you are talking about the competitive tax system and the value-added tax. You say, "If Japan installs a value-added tax, the United States would be left as the only major industrial nation." Indeed, you are right. I think most of Japan's competitors are unaware that as yet they don't have a border-neutral tax, and that it will only make their products infinitely more competitive if they go to that kind of tax, in terms of international competition.

Do you think the United States should go to—it doesn't have to be a value-added tax—some form of border-neutral tax that is rebatable at export and can be charged to imports?

Mr. LEEDY. It seems to me to be the most straightforward way of equalizing or normalizing the tax effect of international trade transactions.

Yes, Senator, I would strongly support the idea that we try to put our industry on the same footing from a tax perspective as industries in Europe and in Japan.

The CHAIRMAN. You may have the intelligence I do; I am led to believe that Japan is going to go to it in 1987, significantly reducing their taxes on income and capital and shifting over to some form of border-neutral consumption tax.

Mr. Davis, what do you think about that idea?

Mr. DAVIS. I concur. I think we have to see ourselves operating in an international economy, at least in the field of high tech. We are in an international economy, like it or not, and we have to move in that direction.

The CHAIRMAN. I can ask both of you, but I will start with Mr. Leedy: You know the complaint we are now getting from some of the chip manufacturers in this country about they are now unable to compete in this country—forget, for the moment, foreign markets—in this country with foreign competition. How on earth do both of your companies, because you pay good wage rates, how do you manage to stay perpetually one jump ahead of foreign competition—confine it to this country if you want—and are faced with wage rates that are clearly in many areas a fraction of what you are paying?

Mr. LEEDY. Well, the answer that we have sought at Tektronix is to continue to invest, Senator. And as I indicated earlier, as my statement reflects, those investments are very heavy; they are not only a substantial portion of our net sales, they are many times the amount of our annual net after-tax earnings, our investments in research and development.

It is only through that kind of continual development of the products that we can hope to stay ahead.

I might add, parenthetically, that what I saw in yesterday's paper about the potential for elimination of the investment tax credit would be a setback of substantial proportions.

The CHAIRMAN. And somewhat of a limitation on the R&D credit.

Mr. LEEDY. And likewise, it would be a major setback. We strongly support the idea that the R&D credit be continued, and indeed that it be expanded for this purpose.

The CHAIRMAN. Go ahead, Charley.

Mr. Davis. Well, I concur, but I guess my response with respect to competition is that it ain't easy. It takes a tremendous amount of our resources, in terms of at least 10 percent every year of our sales dollar into research. But in addition to that, it takes a lot of hard work on the part of a very dedicated staff of people, year after year after year, to know that the competition, we may not be able to see them out there but they are out there, and we hope to stay ahead of them. The only way that is going to be done is by very diligent effort.

The Chairman. And you are convinced that American ingenuity, American know-how, American inventiveness, can forever stay ahead of the same qualities in foreigners, even with the wage differential? No matter how bright they are, no matter how advanced they are, we can stay ahead of them on productivity, stay ahead of them on capital investment, invention, and maintain our market shares?

Mr. Davis. Yes, but not if we relax and back off with the educational system; if we relax and decide that the American ingenuity of the 1920's is going to supply us with a market forever, we are going to be in trouble. We have to work a lot harder than we are today every day in the future, we have to educate a lot better every day and every day in the future, in order to stay ahead of that competition.

The Chairman. Mr. Leedy.

Mr. Leedy. I think I concur with what Charley says, Senator. I think that we have been able to achieve these results with this kind of hard work. We are ahead today. Our research and development, and our technological capabilities are, I believe, superior to those of our foreign competitors.

I think the factors upon which our ability to stay ahead depend are the ones that have been outlined here.

The Chairman. There were two other things in your testimony, Mr. Leedy, that struck me. One was on productivity: "Our productivity has increased from $44,000 per employee in 1981 to $70,000 this year." Then, in reference to the statement Mr. Davis made about education, and I am quoting here from Mr. Leedy's statement, "Our employees in academic year 1984-85 were reimbursed more than $9.3 million in tuition costs for educational programs."

I assume that is mostly local education costs. These are not Harvard MBA's, by and large, these are people going to Portland Community College or Portland State, or something like that?

Mr. Leedy. That is exactly right; a substantial number of the courses sponsored by local institutions of higher learning are even conducted in our own facilities.

The Chairman. The reason I emphasize that is, we are having a debate over the extension of that particular employee benefit; it runs out at the end of this year. I have maintained over and over, if we are going to be trimming, as we are, our expenses for education, governmental expenses for education, and if we are going to expect employers to pick it up and stay competitive, this is probably one of the best bargains we get for the money. And certainly if we eliminate that employee benefit, and that tuition becomes "income" to the employees—if you pay for them to go to Portland Community College or to Portland State—it doesn't simplify the system; you have got to withhold, they have got to pay taxes on it, and my hunch is it is going to be a deterrent for the kind of education that both your companies need to keep yourselves slightly ahead.

Senator Baucus.

Senator BAUCUS. Thank you, Mr. Chairman.

Gentlemen, I appreciate your focusing on the second question, the second of the three posed, that is, "Can you compete but with fair competition?" But that somewhat assumes the answer to the first question—that is, what is fair, and what is unfair?

So, my question to each of you is: Are there any trading practices engaged in by any other countries which you think are unfair and should be changed? And, if so, what are they?

Mr. DAVIS. Well, I think the ones that we would object to are ones where I have no idea how you could effect legislation to change them. We think folks who are copying the products that we made 10 years ago shouldn't do so, but they should buy a new one.

Where our products are looked at in Japan, and the thing we are making 10 to 15 years ago is copied and sold in competition with us, we would prefer that not happen. But we see that as part of the marketing requirement for us to persuade our customers in Japan that they ought to have this year's model and that we ought to demonstrate that it is better than the one we stopped making.

Senator BAUCUS. You are talking about reverse engineering and intellectual property rights?

Mr. DAVIS. That's right. But reverse engineering is something that I see no way of having the Congress prohibit.

Senator BAUCUS. Are there any other unfair practices that leap out, that jump into your mind, that should be stopped?

Mr. LEEDY. I might say that we have seen some instances of patent infringement involved in products sold in this country, and I think that the remedies for that are rather cumbersome. There are opportunities in connection with commercial sales to exclude infringing products, of course, under the trade laws at the border. There are, however, much more limited opportunities where the U.S. Government is the customer for those products.

I have no recommendations, really, to offer on that subject. We have not been, in my tenure at Tektronix, we have not been noticeably affected by blatant dumping by foreign competition. If we were, I would judge the remedies, again, to be somewhat cumbersome and somewhat expensive to undertake.

I don't know if I am being responsive, Senator, to your question.

Senator BAUCUS. To what degree are you a specialty company in the semiconductor industry? I ask the question because many people in the semiconductor industry say that one unfair practice is the inability of American companies to market and sell in Japan; that is, we have 50 percent of the market worldwide, and we have 10 percent of the market in Japan. And even though Japan eliminated its tariffs in 1975, I guess it was, which is on the surface opening up its market, the fact of the matter is that our market share there is still 10 percent, the argument being that we need to sell in Japan because that is a big market, in order to get economies of scale and bring costs down, and also to be able to generate the cashflow necessary for R&D and to develop new technologies.

My question is: Are your firms—to some degree, I don't want to overstate the point—specialty firms that are carving out a niche in the general semiconductor industry? Or are you in the same boat as everybody else and you just disagree with the vast bulk of semiconductor firms, which claim that it is unfair of Japan to not grant full access to American companies? The argument is that Japan and various other purchasers have cross-purchase agreements in Japan to buy from each other and therefore effectively deny American companies from selling in Japan.

Mr. LEEDY. Well, I think our experience in Japan is somewhat different from that of the general semiconductor companies. Tektronix went into Japan 20 years ago in a joint venture with Sony Corp., and it has been an enormous success. Japan is an important market to us. Our products have been important in the industry in Japan. We have a very significant position there.

That gives my company a somewhat different perspective on this issue than those who have found their markets closed, and I don't doubt that they have. I would say, though, that for both companies like ours and companies like the broader generic semiconductor manufacturers, the issue really is to find a way to open those markets in Japan and have access to them.

Senator BAUCUS. Now, why have you been able to, and why have others been unable to, open those markets? What is the difference? What explains the difference?

Mr. LEEDY. Well, I would like to take credit for my company for the success that we have had in focusing on that market and offering products which were needed and accepted as industry standards in Japan. I think certainly our development of unique products has played a major role in that. I think our approach to the market through a joint venture, through a partnership with a Japanese company, has played a significant role. And I guess I would also say that the fact that our products are used as a part of the infrastructure of the electronics industry to engage in research and development, they are tools for engineers, made it fairly obvious to our Japanese customers that they needed those or something like them in order to build their own industry.

Senator BAUCUS. I see my time is up.

The CHAIRMAN. Senator Moynihan.

Senator MOYNIHAN. I would like to thank Mr. Davis and Mr. Leedy for raising a question which, to my knowledge, has not yet been discussed in this committee, and which has played almost no part whatever in our deliberations on trade which is American-imposed restraints on exports.

The degree to which we inhibit our own producers from exporting because of our own restraints seems to me to be the least examined of our trade issues. There is a whole network in Washington of people who say, "No, you cannot sell that abroad."

In inviting comment, let me just say I have two senses. One is that export regulation is likely to be the most bureaucratized of government functions. This may be unfair to some very fine civil servants, but I cannot imagine a technologically innovative person wanting to spend his time saying, "No, you can't sell that abroad."

Secondly, it smacks of a kind of primitivism, of a feeling that there are secrets about the world which you can keep from other people. Technology is a culture, it's not a secret.

When I was a boy it used to be said that the Japanese had stolen the plans to one of our battleships. That is something that every kid on my block knew. It wasn't until I grew up and got to be aboard a medium-sized U.S Navy vessel that I realized that the plans to an American battleship would take up about 15 railroad cars, at a minimum. Now, you don't steal plans to a battleship.

But would you speak to that, gentlemen, both of you? Shouldn't we inquire more into this? What do you run into? Who tells you "No," Mr. Davis?

Mr. DAVIS. That is part of the question.

Senator MOYNIHAN. Ah, yes. That, too, is classified. [Laughter.]

Mr. DAVIS. Now, it is difficult to discuss this issue without appearing to malign persons who are doing their jobs as conscientiously as they know how.

Senator MOYNIHAN. Doing what they are asked to do by the Government.

Mr. DAVIS. And are doing the things that are necessary for the organization to function. But I think a key factor in the misperception of the OEA, about its role, is its failure to see that facilitating trade has to be a value down the line some place. If the OEA sees its job as denying licenses, if their motivation is somehow compensated by the number of licenses they deny this month or by the number of general export licenses that they withdraw, then it strikes me that that is the wrong motivation.

If they see, as well, the need for getting out of their system all of the products that really are not products they should be controlling, enabling us to get into the marketplace with our products without them on our backs, that would be helpful.

Now, as you go through the system day after day, unless you have a person located in Washington, DC, full time, you will find that you will have to send somebody to Washington to find that export license and move it through the system. And very frequently, just finding that piece of paper is almost impossible.

I know what my airline reservation is to get back to Oregon this afternoon. I can't possibly find out where an export license is that we submitted 10 to 15 days ago in the export administration, unless I go over there. The failure to computerize that organization, it seems to me, is a major—a major—factor in the delay of licensing.

Senator MOYNIHAN. Mr. Davis, you are telling us that the organization responsible for keeping high technology secrets out of the hands of the Taiwanese is still using paper files? Well, they are right on the cutting edge. [Laughter.]

Mr. DAVIS. Well, if they haven't improved their system since a telephone conversation this morning at 8 o'clock. A letter that we sent them on October 23d, I think it was, followed up by a copy of that letter that we submitted to them on November 7, we will take copies of that letter and all the documents back over there this afternoon, so that they will have them, again, in order to make a decision that has already been made informally—that is, we have been told that certain of our products are no longer subject to control. We were told that I think it was October 23, several weeks ago or quite a while ago, anyway.

Senator MOYNIHAN. Sir, my time is up, but may I say that I think, Mr. Chairman, this is a subject we cannot just let go by. We have to have these people in and talk to them.

I think Mr. Davis and Mr. Leedy have made a very important contribution. And it never hurts to look at your own behavior before you start blaming others. Obviously we have a clumsy situation here that, at a minimum, needs closer examination.

Is that not right, sir? Can I get some assent from the Chairman, before my moment goes by?

The CHAIRMAN. You are right. This committee has not dealt extensively into the Export Control Act, because it is the Banking Committee's jurisdiction. But every company that comes before us that is involved in international trade raises this question. It is not unique to these two companies, it is not unique to Oregon. I have not run across a company in this country that does not have a horror story almost identical to what Mr. Davis and Mr. Leedy have referred to.

Senator MOYNIHAN. Maybe we could buy them some cheap Japanese hand calculators. [Laughter.]

Mr. DAVIS. Right.

Senator MOYNIHAN. Thank you Mr. Chairman.

The CHAIRMAN. Senator Wallop?

Senator WALLOP. Mr. Chairman, in addition to finding a problem in the bureaucracy of our government, which all of us knew to exist, we have just demonstrated the problem of the Congress, too, because it is not our reach. You know? We develop the problem, but we don't reach it, and it is one of the major frustrations I have had on a number of issues that have come in front of this committee, not the least of which is tax treatment of donations to national parks. We can't get those two budgets into the same box to deal with it; which is not the subject of this hearing, but I hope that maybe as we view this perhaps we could engage the other committee in a joint hearing, or some such arrangement, to at least beging to put the problem in some perspective.

I take it that neither of you quarrel with the concept, though, that some U.S. technology does have a national security interest which ought to be protected.

Mr. DAVIS. No quarrel at all.

Mr. LEEDY. Absolutely.

Senator WALLOP. I think that seems to be an acceptable concept. The question is getting clean decisions in orderly periods.

Mr. DAVIS. Yes. And beyond that, we are in a technology that moves very rapidly; so that, the ordinary legal mind, if you will pardon that phrase——

Senator WALLOP. It doesn't trouble me; it may trouble a few here, but it doesn't trouble me. [Laughter.]

Mr. DAVIS. Which says that we will publish proposed regulations and then we will go to hearing, we will have 90 days for a hearing, and then we will adopt those regulations within the next 6 months—well, that is about 9 months out of phase, because we need it in this environment. In the competitive worldwide environment, the technology moves much more rapidly than the usual process of adopting rules and imposing those on the industry.

I think the controls have been to be accelerated very much with the perception that we are in an international economy; we are not in a plodding U.S.-protected economy at all.

Senator WALLOP. You know, that is such a nice, refreshing thing to hear, and I think a lot of us recognize it. If one were to be able to surface this problem in any kind of an effective way from the congressional standpoint, would there be any benefit in trying to get the variety of industries whose products are the most likely subject of question as to national security involved in redesigning a process that could deliver the decisions?

In other words, would you all, do you think, as sort of respresentatives of a variety of American industry, be willing to come to some kind of a conference that designed a process whereby decisions could be made more rapidly?

Mr. DAVIS. Well, certainly, if we could be of any assistance, I'm sure.

Senator WALLOP. Well, I agree that it is hard to assist the bureaucracy. Nobody ever had any trouble getting a bureaucracy to do nothing; but it seems to me in the national interest that we get the involvement of the people who have an understanding of the fact that there is a national security problem, and that that is a relevant thing for a country to look to. But the other relevant thing is survival in the rest of the markets.

It strikes me that we are going to have to look at the whole process that we have set up for public involvement. You know, Congress has already said that you have to have public hearings, and that there has to be a period for comment after rules are proposed; so, we are every bit as much of the problem as the bureaucracy that we glibly criticize here. It seems to me we are going to have to do some things in this area as well.

The CHAIRMAN. Well, you have heard about the new game, "Bureaucracy"—the first person to make a move loses. [Laughter.]

Senator WALLOP. Mr. Chairman, let me ask just one question of Mr. Leedy, because I see my time is nearly up.

Your company has a number of Occidentals who speak Japanese, do they not?

Mr. LEEDY. Yes, although I suspect that the language capability we have is more with people of Asian descent. There are not many Occidentals who speak Japanese, even on the west coast.

Senator WALLOP. It is a big problem in this country, as we seek to compete with other countries who do take the time to give language training and have their people involved immediately in cultures. That is not a corporate failing, it is an educational; pasttime in which we don't indulge ourselves.

But it just strikes me that I want to compliment you, and I think that your testimony is valuable to us, to know that 20 years ago you had the foresight to find out how to enter a market and become a major part of it.

A lot of our problems as I see them are clearly the recognizable real ones that have been recited; but a lot of them are, additionally, just an American sort of sloth in the world of competition. We have had it our way so long that we are not used to having people beat us at a game that we once excelled at. So, I just want to say that I appreciate that testimony as well.

Mr. Leedy. Thank you very much.

The Chairman. Are there any other questions?

Senator Moynihan. Mr. Chairman, could I just make this point? Mr. Davis mentioned the question of what are the interests of organizations. It is not hard to look at techniques of organization maintenance. The measure of an export-control organization's product is more likely to be the number of times they said no than the number of times they said yes.

And you can look at these things like you can look at circuitry and make a judgment, and if that is what we have got ourselves into, we ought to try to get ourselves out of it.

Mr. Davis. I agree. Thank you.

The Chairman. Senator Bradley, any questions of these witnesses?

Senator Bradley. No, Mr. Chairman.

The Chairman. Gentlemen, thank you very much, good to have you here.

Now let's move on, if we can, to Professor Jackson, and then we will move on to the panel of Hufbauer, Lawrence, and Aho.

Professor, go right ahead. We're glad to have you with us.

STATEMENT OF JOHN JACKSON, HESSEL E. YNTEMA PROFESSOR OF LAW, UNIVERSITY OF MICHIGAN, ANN ARBOR, MI

Professor Jackson. Thank you, Senator.

I am one of those "ordinary legal minds" that was referred to a few minutes ago. [Laughter.]

I just have a few brief summary comments to make that are embellished a bit in the written statement.

So let me just focus on two things; but first, let me say something that you all know very intimately already, but I want to say it to set the stage of where we are.

We have today a major problem of how to manage interdependence. Forces of economics flow very quickly from one economy to another, and this is a considerable source of frustration for national leaders who try to effectuate policies that carry out programs for their constituents.

But to a large extent this situation is a product of the success of the system that was put in place just after World War II. The GATT is at least partly responsible and indeed praised for reducing or enabling the reduction of a large number of barriers to trade among nations. When you get into a situation as we are in today, where at least as to the industrial democratic countries, and at least as to industrial tariffs, those tariffs have very little impact at all. This is part of what has created the interdependence. So, what we have to do is, we have to go on to the next phase. We have to begin to think about how we are going to handle this interdependence.

Addressing these questions, I basically have looked at two issues for today's hearing, and I will describe those but, of course, I am open for questions on a broader range of issues, as you wish.

The first point that I would like to make is illustrated by one of two exhibits that I have in the testimony—it is exhibit No. 1 near the end of that testimony. It is an analysis based on what economists call "variable costs." It is easy to see why economies that are as different as the United States market economy and a Soviet Union nonmarket economy have difficulty trading together. It also is easy to see why economies on the one hand that are industrialized and on the other hand are developing have trouble trading together. What is often overlooked is that rather minor variations in economies that are very similar otherwise can pose some difficulties, and I think in many cases those difficulties are not intentional.

So, when we use the terminology "fair" or "unfair," we may be somewhat misrepresenting at least part of the problem,

And this case that I pose in exhibit 1 illustrates that. This case suggests two economies and one industrial sector. If you would like you may think of Japan and the United States and the steel sector; but I don't claim the facts in this exhibit necessarily are identical to the actual reality.

In Japan, several of the characteristics of that sector are that workers tend to have tenure—that is, they are not easily laid off—and there is usually a high debt/equity ratio, sometimes 90 percent debt.

Now, what this basically means is that the fixed costs of that industrial sector in that foreign country are much higher, as a percentage of the total costs. You have to pay your interest anyway, whether you are producing or not. If you view it important to keep your workers employed, you have to pay their wages, anyway, whether you are producing or not.

The contrast could be with an industry sector in the United States, where we do not have worker tenure, at least as prevalent, and we may have a much different ratio of debt, much smaller ratio of debt, which at least in some circumstances means that dividends can be skipped, so that dividends could be called "the variable cost."

Now, if you have a situation of declining economic demand, the economists will say a company is rational to produce and sell at anything over its variable costs.

Because of these circumstances, which may not at all have been engineered for this purpose, the variable costs in this case of the foreign sector are much, much lower because the fixed costs are much higher.

And so, I pose the question in the exhibit: Is that an unfair action? Or is this something that I have sometimes called "a problem of managing the interface of the economies in today's interdependent world?" Do we need some kind of a mechanism for managing that interface?

That's a partly rhetorical question. Obviously, I think we do need an interface mechanism; the question is whether the system we have today, the GATT system, our national laws, dumping, countervailing, and so on, are an adequate response for that goal. They do have some effect, but they may be a rather blunt tool.

So much for my first point.

The second point deals with what I think is the most significant problem of trade policy today, and that is subsidies. (See exhibit No. 2) We are all very perplexed by subsidies. I continue to be preplexed. I may not be able to give you as much guidance as you might hope in your questioning, but I will try to give you some of my thoughts on that, which are still evolving.

The problem of subsidies often is divided into two kinds—the so-called "export subsidies," i.e. subsidies just for exports, and "domestic subsidies." There are a variety of valid reasons why we want both the international and the national system to respond in some way to subsidies in world trade, either by making international obligations prohibit certain kinds of subsidies, or by a unilateral national response called "countervailing duty."

The problem is, for these purposes what do you call a "subsidy"? And as soon as you talk about domestic subsidies, you get very deeply entwined into national government policies and "national sovereignty." No government does without subsidies as a tool of government. There are a variety of reasons why subsidies are used: to redress inequalities of income, to redress the harm and hurt of poverty, to pursue certain goals—in some countries they might be religious goals, they might be cultural goals, or economic goals; but, presumably, at least in some countries, they are democratically decided upon, and that is an attribute of national sovereignty to make those decisions and pursue them.

So, the problem we have is balancing two conflicting goals. On the one hand, a goal of giving national governments the opportunity to use an important tool of government for legitimate governmental purposes; and, on the other hand, to try to prevent the subsidies from distorting world economic forces, distorting them in a way that will reduce the broader goal of a higher world welfare.

So what do we do? Well, as soon as we begin to try to respond with, for example, countervailing duties, we get an enormous definitional problem: What are subsidies? And if you push the definition of subsidies for this purpose very far, if you push it as far as some economists would do, as a matter of fact, talking very broadly about any benefit conferred by a government, you get into virtually every activity of government. Fire and police protection can be a subsidy because, among other things, it will reduce the insurance cost of producing goods. Roads and schools will be subsidies.

So we get into line-drawing, and this has led me to suggest that what we need to do is to think in terms of a subset of subsidies. For want of a better terminology I use a sort of lawyer's term; I call it an "actionable subsidy." We recognize that a broad definition of subsidies can cover a myriad of activities. What we need to figure out is which among those subsidies, which subset among those subsidies, are actionable, in the sense that the international or national system ought to respond to it? And it seems to me that is what we have to try to focus on.

Now, just to wind this up, I suggest a few principles, in the paper, of what might be a beginning of formulating a series of policies for defining actionable subsidies. Some of those principles we already tried to effectuate.

One that has not been often mentioned but, I think, could be very important is that we ought to focus more directly on the question of when subsidies actually have an impact across the border of a country.

Sometimes we seem to be talking about a countervailing response to subsidies, even when they may not have an impact across the border. For example, certain kinds of regional aids may have a distorting effect within a country. You can argue, however, that that is a sovereign decision of that country, to take somewhat less welfare for some other objective. If it does not have an effect at the border, however, or across the border, upon neighboring countries or upon trading partners, then, arguably, we should not respond to it.

I think, Mr. Chairman, I will just stop there.

[Professor Jackson's written testimony follows:]

TESTIMONY BEFORE THE FINANCE COMMITTEE OF THE UNITED STATES SENATE

November 21, 1985

By John H. Jackson
Hessel E. Yntema Professor of Law
University of Michgan

SUMMARY OF PRINCIPAL POINTS

1. Interdependence reduces sovereign independence and frustrates national governments and leaders in their attempts to carry out programs on behalf of their constituents.

2. To a large extent the current conditions of interdependence result from the success of the Bretton Woods system which includes the GATT.

3. "Unfair trade laws", are based on the policy of the "level playing field" and market economic principles. Not all nations agree with these principles.

4. Major differences in economic systems, such as between market and non-market economies, or developing and industrial countries, can create problems in trading relationships. But even relatively minor differences between two similar countries, such as two industrial market democracies, can by coincidence create situations which appear unfair and cause tensions and disputes. We need to think of some of these situations as requiring an "interface" mechanism to assist such nations to trade amicably together.

5. Subsidies are the most significant problem of current trade policy. They are deeply intertwined with national sovereignty. International rules on domestic or general subsidies often involve balancing legitimate national government policy goals with the "level playing field" policies. Consequently a set of rules to help accomplish this balancing, is important. These rules include an injury test, and various principles of excluding from international consideration subsidy-like practices which either do not have an effect across borders, or are de minimus. The specificity test would be included.

TESTIMONY BEFORE THE FINANCE COMMITTEE OF THE UNITED STATES SENATE

November 21, 1985

By John H. Jackson
Hessel E. Yntema Professor of Law
University of Michgan

I

"Interdependence" may be an overworked word, but it accurately describes our world today. The U.S. depends on exports and imports for an increasing percentage of its national economy, and many other countries have a much higher dependence on trade. Under these conditions, economic influences flow with great rapidity from one country to the next. Thus despite all the talk about sovereignty, independence, and equality of nations, these concepts are fictions if used to describe today's real world. What is the sovereignty of the government of a country whose trade is so dependent on a neighbor that it cannot set its own interest rate, specify its own tax system, or design its own program of incentives for business or talented individuals? As a result there is much frustration among governments and their leaders. Most governments find it difficult to carry out their program goals on behalf of their constituents, such as providing full employment, or increasing economic benefits.

To a great extent the international economic interdependence of today can be attributed to the success of the institutions put in place just after World War II, what I will losely call the Bretton Woods System, which includes among others the IMF and the GATT. To be sure, decreases in the costs of transportation and communication may have had the largest role, but without the rules of the Bretton Woods system governments could easily have acted to negate many of those advantages. The efforts of the GATT over 38 years, for example, can be praised as the cause of the dismantling of un-economic tariffs on trade in industrial goods, at least among the democratic market oriented industrial countries.

This success has caused us to face a new set of problems.

With the decline of tariffs almost to irrelevancy, other much more complex barriers or distortions to trade appear to be relatively more important. Non-tariff barriers are myriad, and the ingenuity of man to invent new ones assures us that the problem of trade barriers will never go away. This is why one of the most important problems facing us is institutional -- the question of whether national and international governmental institutions (such as GATT) have the capacity to meet the challenges of private and governmental behavior which could impose great risks on the inter-linked trade and investment world in which we find ourselves.

II

You have asked me to address particularly the problem of what is "fair" or "unfair" in today's international trade practices. As the focus has shifted from tariffs responding to fair trade, or even from escape clause or so-called safeguard practices also responding to fair trade, enterprises troubled by foreign competition have increasingly turned to the unfair trade laws for relief from that competition. In many, perhaps most, cases it is appropriate that they do so. It must be recognized, however, that in some cases attempts are being made to respond to practices abroad which are unfair only in the eyes of the domestic industries which would like freedom from the challenges which competition brings. There is an increasing number of situations which involve very difficult balancing of contradictory economic, cultural, and political goals.

The essential policy behind unfair trade practice rules is the notion of the "level playing field." This is the idea that enterprises should be able to compete in the open markets of the world on the basis of market economic principles which apply equally to all participating enterprises. Unfortunately we are well aware that many societies do not have the affinity for market economics which we in the U.S. do. Thus, at the very base of the idea, we are troubled by deep and fundamental differences of opinion about the appropriate economic role of governments.

I cannot comment about all of the many rules regarding "unfair trade." Instead I would like to use an hypothetical example to illustrate the conceptual problem of applying some of them. Then I would like to comment on what seems to be the most difficult current trade policy subject -- that of government subsidies and the appropriate responses to such subsidies. I have brought with me several exhibits designed to help me make certain points about these.

III

It is reasonably obvious that nations with very different economic systems are likely to have some difficulties in trading together. For the United States, with its market economy, to trade extensively with a non-market country like the Soviet Union, presents a number of problems. Enterprises in the U.S. reasonably worry whether they are facing competition which is essentially underwritten by the government of the non-market economy. The international rules such as those of GATT, were not well designed to govern such situations.

Likewise, an industrial nation will face problems in trading with a developing country. Low wage rates, as well as many non-market features of the developing country's government, can impose considerable adjustment strains on the industrial society. On the other hand the developing country worries about the strains which high efficiency and high technology can impose on it through imported goods.

What is often surprising, however, is that even nations with very similar economic systems, such as two industrial country market economies, can find that minor variations in their economic systems can create situations which have the appearance of unfairness. These situations may have arisen almost completely by accident. That is, there may have been no intention to engage in any practice which is deemed "unfair", or which appears to shift burdens such as unemployment or adjustment onto another society.

Let me illustrate this with Exhibit 1. In this exhibit, a situation is posed which is based on trade between moderately different economic systems. The fact that in an industry in one society a higher portion of average costs are fixed costs, means that it has lower variable costs. In times of slack demand, enterprises of that industry will rationally seek to continue producing if they can sell at any price which will be slightly above their variable costs. Under conditions of liberal or free trade, such low variable cost society will very likely export extensively to a society with higher variable (i.e. lower fixed) costs, thus causing adjustment and unemployment in the latter. This is so even though long term average costs in both societies are the same. Is this "unfair", or is it a coincidental (but real) problem which the two societies should try to solve with a buffering mechanism which minimizes administrative and advocacy costs as well as moral terminology?

In some of my writings I have termed this problem the "interface" problem. This word draws on the terminology of computer technology. When it is desired that two computers of different makes work together, it often takes some kind of "interface" mechanism or program to mediate between them and to translate the language of one machine to that of the other. Likewise when two societies with even minor economic differences desire to work together, frictions or misunderstandings can occur unless there is an interface mechanism. To a certain extent, the national trade laws and the GATT-Bretton Woods System are operating today as a rather crude interface mechanism. The problem often is that policy leaders have not perceived this, but instead believe that it is necessary to characterize some practices as "unfair" or "illegal". In at least some of the international trade problems which exist today, a more neutral terminology and policy approach that would avoid moral overtones may operate with greater utility for world economic welfare and harmony.

It may be that to a certain extent the anti-dumping rules and/or the subsidy rules are performing this interface function, although with much administrative cost and overtones of moral indignation that may not always be appropriate. With respect to the anti-dumping laws, incidentally, it must be recognized that they are based on policies very analogous to our domestic price-discrimination laws, and that there have been important criticisms of those policies. Many economists suggest that price discrimination by an enterprise is not only not unfair, but can have a pro-competitive effect which strengthens an economy.

IV

I believe that the most important trade policy problem today is that of subsidies for goods which move across borders. This includes not only the pure export subsidy, but general or domestic subsidies benefiting all goods of a particular type which are produced in a society, whether or not they are exported.

Sometimes it is suggested that imports of subsidized goods ought not to be a subject of concern. Indeed the consumer or buyer in the importing country clearly benefits from the subsidy. Thus it is said that such country should send the export country a "thank-you note."

I do not join this viewpoint. First, it does not adequately take into account the broader world perspective by which economists demonstrate that subsidies have a distorting effect on market economic principles which tends to reduce world welfare.

Second, subsidies could in some cases have a predatory intent. They could be used to assist an industry to gain foreign market share, with a view that after driving out foreign competitors, prices could be raised to capture so-called monopoly "rents." Even if this is not the case, there still is the legitimate worry that when the subsidy begins, it can cause adjustment costs in the importing country. When it ends it can again cause such costs, and these costs can be substantial, possibly even rivaling the benefit to the importing society from the subsidy itself.

Third, and more subtle, subsidies on imported goods can have an effect on the efficiency and initiative in a market economy, by adding to the risks of innovation, small business start-ups, and general entrpreneural activity. The businessman sometimes says that he can compete against fair trade, on a level playing field, but he cannot compete against the deep pockets of a foreign finance ministry with government taxation at its disposal. Even if these fears are exaggerated, nevertheless a subsidy offered by a foreign government may be designed to shift political burdens to foreign countries, as the exporting society struggles to maintain a majority in its parliament by propping up sick industries in key constituencies. One approach is for the importing country to "counter subsidize", but in doing so it may be simply altering its own economic system. Why should an exporting nation be allowed to impose such changes on an importing nation?

All of these arguments have led statesmen for a century to recognize that international rules are needed to limit the uses of subsidies in international trade, and that importing nations should be allowed a unilateral permitted response of a countervailing duty to offset the subsidy effect of imports. The really tough question, however, is how far to take this principle.

If the word "subsidy" for these purposes is used in a broad sense, such as some economists use it to indicate any economic benefit furnished by a government, the result becomes absurd. Even good fire and police protection is a subsidy in this sense, since it reduces the insurance cost of producing goods. Roads and schools likewise can be called subsidies. Soon importing societies could be countervailing right and left, with grave implications for the policies of liberal trade.

Consequently it is clear that it is very important to draw some border lines around the concept of "subsidy" for trade policy purposes. I prefer to think in terms of a sub-set of activities within the universe of broadly defined subsidy, which I would term "actionable subsidies." These "actionable subsidies" are the only subsidizing activities to which the international and national trade rules should respond. The critical question then becomes defining a set of rules which can identify which subsidies should be considered "actionable".

This is no easy task, however. In the case of export subsidies it may be relatively easy. Usually such activity has an apparent motive of shifting certain kinds of political or adjustment burdens to other nations and arguably should be prohibited or at least countervailed, possibly as a "per se" violation of the rules without benefit of an injury test.

Domestic or general subsidies are another matter however. Such subsidies are an important tool of government policy. They are used extensively by all governments, and often for laudatory policy goals, such as redressing unfair imbalances of income, alleviating distress of poverty, or pursuing democratic priorities of various types such as cultural, religious, national security goals. They are mixed deeply into the fabric of national sovereignty. In these cases, the objectives of international trade rules to minimize market distortions must be balanced against the competing legitimate government goals.

One way this is done is to provide an "injury test" as a prerequisite for unilateral countervailing duties of an importing nation. As long as the subsidies on the imports do not in fact cause a sufficient threshold injury to the competing industry of the importing country, no countervailing duty response should be permitted. This is essentially the structure of the international and national rules on the subject. However the importance of the injury test as a mediating or "interface" mechanism between two opposing and equally legitimate policy objectives is sometimes forgotten.

In my Exhibit No. 2, drawn from some materials I use in my courses, I have set forth a large number of specific subsidy like practices. Some of these practices should clearly be designated as "actionable subsidies." Others should clearly not be so designated, because they are common activities of governments, and because they have so little distorting effect. Other practices on the list illustrate how deeply entwined into the fabric of society are certain activities which could be called subsidies. In an inappropriately broad sense of subsidy, even bankruptcy, or social security could be swept into the category of "subsidy".

The United States has become far and away the largest user of countervailing duty procedures. All other nations combined have probably not used countervailing duties explicitly to offset subsidies on imports more than about two dozen times. Yet since the 1974 Trade Act, the United States has had about 250 petitions for countervailing duties, and found affirmatively so as to apply such duties in approximately 30 cases. As I mentioned above, there are good policy reasons for this approach. But the U.S. is blazing a trail. Its administrators have had to face tough questions well in advance of international agreement on many subsidy issues. Because of its economic importance, the U.S. actions have an asymmetrically weighty impact on the trade of our partners.

Countervailing duties applied by many small nations would have essentially no impact. Such duties by the U.S. can have serious impacts on foreign national policies, economic welfare, debt service capability, and political stability. This imposes on the U.S. important responsibilities, which some of our trading partners are not certain we are prepared to fulfill. We need to proceed fairly, and in a principled manner. We need to avoid the processes themselves becoming burdensome out of proportion to their benefits. We need to be prepared to discuss and enter into international agreement on many of the subsidy issues, and to submit as well as demand others submit to objective dispute settlement procedures concerning these issues. We need to be able to implement into our own legal system the results of these agreements and dispute settlement determinations (a question on which there is some doubt.)

In conclusion, let me suggest a few principles which might form part of a larger set of rules designed to help define the border lines of "actionable subsidy" in a way which appropriately balances the various conflicting policy goals of giving maximum possible freedom to national sovereigns to pursue goals of their constituents, while preventing international trade activity that tends to shift the burden of those national programs onto other countries. I would suggest:

1) Recognition must be given to the reciprocity and fairness of symmetry of subsidy rules: whatever rules the U. S. follows,

it must recognize the right of other countries to also follow and that therefore such rules may affect U.S. exports as well as its imports.

2) Response to subsidies should only occur when it can be shown by economic analysis that a particular subsidy practice can have an effect across a border. If a particular nation wishes to distort its own economy, or reduce its own welfare by subsidizing some group, that should be considered a national decision not of concern to the international trade system unless some reasonably significant effect on other countries can be shown. In some cases, for example, regional aides would fall in this category when they only shift the location of an industry but do not affect amounts or prices of goods exported. Likewise some natural resource policies may be shown to cause no changes in export amounts or prices, but instead merely to redistribute economic "rents" within the exporting country.

3) Some practices, such as most export subsidies, should probably be defined by international agreement to be "per se" violations of fairness rules, so that a rapid response could be implemented even without an injury test.

4) A de minimus termination at an early stage of cases is important to minimize procedural and administrative costs and to

minimize unnecessary intrusion into the internal affairs of other countries. The current U.S. de minimus level of 0.5 percent is probably too low. A higher de minimus could be the prime facie case, with opportunity for petitioners in certain specific circumstances of low margin goods to show that a lower de minimus is necessary.

5) The injury test is an important mediating "interface" mechanism, and should not be weakened by devices such as cumulation, or departure from a "margins" causal analysis.

6) The "specificity" or general availability test can be a very useful principle to avoid using subsidy response rules for many government practices which are often common among all governments, and which probably have little distorting effect. Roads, schools, fire and police protection, all come to mind. This test needs to be refined and rethought to avoid its inappropriate use, however.

7) More effort is needed to reduce the costs of the procedure and administration, so that these do not themselves become trade barriers. Some principles mentioned above would help.

Exhibit No. 1
Prof. John H. Jackson
University of Michigan
November 1985

VARIABLE COSTS AND THE INTERFACE PRINCIPLE

Assume the following facts: In the same industrial sector (e.g. steel) in two societies (e.g. Japan and the United States) the following different characteristics are present: (No assertion is made that these facts are real. This is an hypothetical case to illustrate a principle.)

Society A:	Worker tenure (no layoffs, etc.) High debt-equity ratio in capitalization (e.g. 90% debt)
Society B:	No worker tenure (worker costs thus are "variable costs") Debt-equity ratio not exceeding 50% (dividends can be skipped)

Examine the implications for variable cost analysis in times of slack demand:

Economists note that in times of slack demand, a firm is rational to continue producing as long as it can sell at or above its short term variable costs (because it must continue paying its fixed costs anyway). Of course this can only continue for limited periods, persumably over the complete business cycle the firm must not incurr losses.

Analysis of short term variable costs in Societies A and B:

Assume: (million $ unless per unit)

	Society A		Society B	
Costs of a firm:(Average prod)				
Plant upkeep etc.	20	fixed	20	fixed
Debt Service:	90	fixed	50	fixed
Dividends (cost of capital)	10	var	50	var
Worker costs (ave workforce)	40	fixed	40	var
Cost of materials (ave)	40	var	40	var
TOTAL COSTS:	200		200	
Fixed:	150		70	
Variable:	50		130	
Variable costs per unit if ave output 1 mil.units (i.e. price needed to produce)	50 per unit		130 per unit	

RESULT if imports from A to B: Plant in B closes. (Is A "unfair"?)

Exhibit No. 2
Prof. John H. Jackson
University of Michigan
November 1985

SUBSIDIES IN INTERNATIONAL TRADE

For each of the following situations, consider:

1) whether the government practice should be viewed as a "subsidy"
2) whether such practice is "unfair" when it benefits exports, so that an importing nation should impose an offsetting duty or other import restraint?

1. Government makes outright grant to a firm to assist its production of widgets
2. Government makes outright grant to a firm for each widget it produces and exports
3. Government makes outright grant to a firm which produces 12 or 15 different product lines, one of which is designed for export
4. Government loans money to a firm which produces widgets for domestic and export sale, on the following terms:
   --- Government cost of borrowing is 8%
   --- Normal market cost of borrowing for comparable firm is 12%
   --- Government loan in this case is at 10%
5. Government purchases shares (makes equity contribution) of firm producing widgets for domestic and export sale - purchase at market price, established by existing market in the shares
6. Same, as 5. except no market exists in those shares, so an appraised value is used
   --- based on book value, and
   --- with no expectation of dividend for 10 or 20 years, and
   --- knowing firm has business difficulties, and difficulty getting capital
7. Widget firm goes bankrupt, writes off most debt, continues in business and produces widgets for domestic and export sale
8. Government makes grants to widget firm for use in encouraging the retirement or relocation of unneeded workers
9. Government makes grants to WORKERS who lose their jobs from widget firm because of business contraction and improvement of machinery, thus saving potential legal or moral obligations of the firm
10. Government makes grants to workers to retrain for new work in a different production; such workers (retrained) then are employed by gadget firm which produces for domestic and export sale
11. Government adds funds to normal unemployment compensation programs, making it politically easier for a widget firm to lay off or retire workers
12. Government builds a road (or port or rail facility) for exclusive use by widget firm, to encourage it to stay in business at its location.
13. Government builds such road/port/rail/airport for use by general public, knowing that heaviest use will be by the widget firm
14. Government upgrades existing road/port/rail/airport facility for greater use by general public, knowing the widget firm will benefit the most
15. Local government gives real estate and corporate income tax relief to a firm for 10 year period to induce it to locate in the locale; firm produces widgets for domestic and export sale.
16. Government heavily supports local college/university programs in

engineering related to widgets; local widget firm produces for domestic and export sale.

17. Government provides funds for special training of workers to be hired by the widget firm
18. Same, except training is done by local technical high school
19. Government makes special law setting a limit on product liability recovery of consumers or buyers of widgets, where:
    - -widget firm produces only for export
    - -widget firm produces for domestic and export sale
20. Government, to promote science and technology, revises its patent and copyright laws (computer programs?) to better favor high tech industries
21. Government does the same as 20, but limits it just for computer chips
22. Government relieves firms engaged in substantial export from some obligations to install pollution cleaning devices
23. Government relieves industry sectors deemed "export oriented" from environmental control problems
24. Government is generally lax as to environmental problems (Brazil?)
25. Government has no minimum wage law, (or workman's compensation law, or OHSA work place safety law, etc. etc.)
26. Government makes grant (or gives other advantages) to firm conditioned on its location in depressed area:
    - --- grant can be shown to just offset added costs of the location
27. Government gives grant or advantage to firm conditioned on other social policy action, such as hiring handicapped or minority workers
28. Government subsidizes production of a basic resource or input commodity (such as coal), which is then sold to a firm (such as steel) which produces for domestic and export sale.
    - --- in one case, "downstream" firm purchases input for less than it would otherwise
    - --- in another case, it can be shown that the buyer firm pays the same for the input product as it otherwise would, (but the "upstream" producer would go out of business without the government aid.
29. Government owns a natural resource (coal, oil, timber, copper) and sells this resource to domestic firms at a price lower then the world market price. These firms produce for domestic and export sales. The government either refuses to sell the same resources to foreign firms, or sells to them only at a higher price.
30. Government owns a natural resource, and forms a government owned company to exploit the resource and use it for making widgets which are then sold for domestic or export purposes.
31. Government owns a natural resource, and sells it to highest bidder amoung domestic firms (only), which in turn use the resource to produce goods for domestic and export sale. The price these firms can obtain on their markets is essentially the world market price for the finished goods, and this essentially determines the amount the firms can bid for the natural resource.
32. Government shapes it defense procurement contracts to enable a firm to invest in the needed R & D to develope a product, which then has spinoff products suitable for domestic and export sale (computers?)
33. Government gives special income tax deductions and credits for firms producing for export
34. The tax benefits are for all widget firms, but only widget firms, and this sector produces for both domestic and export sale
35. The tax benefits are available to all firms, but are shaped as depreciation deductions on capital equipment, so effectively only capital

intensive industries benefit

36. The government owns most or all of the industry; prices are set by bureaucrats (domestic or export prices). Prices on widgets are set low for both domestic and export sale.
37. The government owns a few selected industries, but included is the widget industry which produces for export and domestic sale
    -the government widget industry has never paid a dividend to the government since "nationalization". (The government compensated original owners.)
    -the government has continued to add capital to its wholly-owned widget industry
38. The government provides many housing, medical, and other social benefits for workers in industry, and because of this firms find they can pay less for labor input into the widgets they produce for domestic and export sale.
39. In a particular society, retirement tends to be at an early age (such as 55) but benefits are not too handsome, so there is a large eager labor pool of persons which desire part-time work (up to a certain specified limit)._ Certain industries, (e.g. assembing certain computer components, or enterring textual data at a keyboard) have discovered ways to take advantage of this type of part time labor, which is paid much less than for other workers. These industries export as well as produce for the domestic market.
40. The government provides a more favorable rate of exchange for foreign currency which is earned from exports, than from other transactions.
41. Same, but black market rate is even more favorable for foreign currency no matter how earned.
42. In each case above, a competing nation finds some of its markets in third countries taken from its firms by the exports mentioned above. What should be its reaction?
43. Government has an anti-monopoly law, but is lax in applying it to a particular industry sector, which sector has many exports.
44. Government has an anti-monopoly law, but is lax in applying it generally.
45. Government has no anti-monopoly law.
46. Government has an export tax generally, but exempts from that tax the export of widgets.
47. Government has an export tax on unfinished logs but none on finished lumber. (Similarly for soybeans & soyameal, or coffee beans & processed instant coffee)
48. Widget imports can be shown to have benefitted by foreign subsidies to the extent of just under 0.5%; or 0.1%, or 0.5%. The legal procedures of a countervailing duty case can be shown to cost the foreign exporter about 10% of its gross returns from widget exports to the countervailing country.
49. The World Bank has financed, at concessional interest rates, the development of a widget plant in a developing country which now exports widgets.
50. A government has good fire and police protection in its society, and thus insurance costs for the widget plant are exceptionally low.
51. In a floating exchange rate world, a government grants an income tax advantage at the same level to ALL exports
52. A government has an exceptionally fine school and university system, and its industry benefits from a well-educated work-force.
53. Societal norms favor "worker tenure" and other paternalistic worker benefits, which for some industries including the widget industry seem

to greatly increase worker output and efficiency, reducing resistance to change and strikes.

54. A government has a domestic sales tax of 4%, charged on sale of goods to consumers. Goods can be exported without paying this tax, (usually in wholesale quantities). It is noticed that the importing country can charge a sales tax there.
55. A government has a domestic VAT (value added tax), which taxes goods at each level of finishing (at about 20%). When goods are exported, whatever VAT has been paid is refunded to the exporter. Goods which are imported are levied a VAT (in addition to tariffs) at the same rate.
56. A government rebates to producer-exporters 25% of the income tax which has been paid by the exporting firm insofar as the income tax can be attributed to that portion of the business devoted to production of the goods which are exported.

The CHAIRMAN. Professor, some have argued that low wages are a form of illegal subsidy. Yesterday, two witnesses argued that the low wages result from repressive governments who do everything they can to keep free unions from organizing and thus keep the wages down by government action, and that this in and of itself is a form of illegal subsidy. What are your thoughts?

Professor JACKSON. I don't think I would term that "an actionable subsidy" in today's world. It seems to me there are a series of cultural actions, cultural situations, even economic structures in various countries, low wages perhaps being one, for which international response gets very, very intrusive.

Maybe sometime in the future we can get around to those things, but, I think, right now we've got our hands full with some more obvious kinds of things, even blatant export subsidies or domestic subsidies that you can show really were intended to impose burdens on other countries.

The CHAIRMAN. What most of the industries are complaining about though, when you strip it all away, that are coming before us is the wage differential. And they are at least telling us—now, maybe they are crying wolf, maybe they really think the wolf if there—but they are telling us they cannot compete against the extraordinary wage differential. And that is the principal complaint. Sometimes the industries call that an unfair trade practice: sometimes they say, "No, we know it hasn't been called that, but we can't compete against it."

What is the answer?

Professor JACKSON. Well, I am not the one to ask what the answer is totally; but I will give you some reactions to the type of questions that I ask in that context.

First of all, some of what we are talking about is the difference in comparative advantage. I mean, if some country does have really low wages, maybe we should be taking advantage of those low wages for our consumers and intermediate buyers that want to buy parts and supplies.

But second, if that is the case, then you can go to a totally different set of policies, under the rubric "safeguards" or "escape clause"—that is, fair trade.

If in the process of taking advantage of the foreign comparative advantages there is going to be an adjustment cost within our own country, because we would want adjustment to move to those areas of endeavor where we are more competitive, the Government has a responsibility, I think, to alleviate the hurt, the real pain, that is involved in that adjustment. Some of that can be done with adjustment assistance or retraining ideas—I notice there is a bill on retraining that looked very intriguing to me—some of it can be done by slowing down the processes, the international processes, that are going on through the use of an escape clause-type remedy where you actually depart from the doctrines of comparative advantage for a temporary period of time to slow it down.

Now, I recognize that is a very traditional answer. I am sure I am not surprising any of you with that answer. But it seems to me that is the direction of how one would look at this problem.

The CHAIRMAN. Unfortunately, I don't think anybody on this committee disagrees with you. Whether or not trade adjustment assistance has worked well is another question. Should we try it? Yes. Should we try to make it work? Yes. Should you try to retrain workers? Yes. But the key issue becomes: Are we going to try to save industries that cannot compete against the wage differential? Or are we simply going to try to phase them out gently?

Professor JACKSON. Well, remember you are talking to a lawyer and not to an economist, and here is what my economist friends tell me, and I am inclined to believe them:

First of all, there is often stated the risk and danger that an industry will be wiped out. I am under the impression that that is unlikely. What is likely to happen is that it will contract. It will contract down to where it is beginning to reach those firms that are, in fact, efficient enough to compete internationally. So, there will be a contraction involved.

If we were able empirically to demonstrate that it is likely that an industry would be wiped out, and there were a national security reason why we needed that industry, then that is a whole other question. I think, we just have to recognize those processes of adjustment. In fact, I think we have gained very greatly from them in this country.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. Thank you.

Professor Jackson, what is the role of GATT here? Is there a role? Many people point out that each year a lower percentage of world trade is covered by the GATT. Others point out that protectionist barriers are rising worldwide, not falling. World trade last year, I think, was around 2 percent; the previous year it was much higher. Yet, these are very difficult problems. It is very difficult to get countries to agree as to what is or is not an unfair trading practice.

Every country wants to export; they don't want to import. At least, industries in those countries want to export. They don't want to contend with or compete with imports—underdeveloped countries, developing countries, industrialized, all countries.

Is there a realistic, meaningful role for a new GATT round here to try to reach some international agreement? Or do we just go it alone and try to reach some agreement on a bilateral basis, just do the best we can, just compete out in the big, rugged world and just to the best we can? Is there a role for a new GATT round here, in a realistic way?

Professor JACKSON. Yes, I think realistically there is a role, almost an essential role, for a new GATT round, or a new round. Arguably, you could raise the question of whether it should be in GATT or someplace else.

The GATT, as I intimated earlier, got off to a very troubled start; it was never the institution it was intended to be, but, in fact, it has been rather successful if you step back from the whole picture of 38 years and look at the sweep of what has happened.

But the very success of that—and it is not entirely successful; there is a lot of backing and filling—the very success of that is creating a whole series of new problems. To me, the question is: Can the GATT cope under its current institutional structure with those new problems? And there, I must confess, I have a lot of doubts.

The GATT is billed as a flexible instrument but it is not; it is a very rigid instrument. Its flexibility comes from violations and departures from the GATT, really.

I think what you are referring to in terms of the trends of trade are perhaps more than anything else the question of whether trade is moving under an MFN regime, that is, a nondiscriminatory regime. And there are a number of indications, although I do not have my hands on good empirical evidence of this, but there is a judgmental conclusion that many people make that we have been more and more departing from the MFN nondiscriminatory regime of trade—a variety of preferential arrangements, the United States perhaps now moving toward a bilateral approach instead of MFN, and so on.

Some of that is frustration with some of the downside arguments of MFN—that is, MFN plays into the hands of the foot-dragger; it is vulnerable to the person who is willing to hold out or the country that is willing to hold out.

So, indeed, I think an argument can be made that certain kinds of departures from MFN—for instance, what we might call code conditionality; that is, giving the advantages of a code only to those countries that are willing to accept the obligations of them—has an important policy role to play in today's world.

Then you get into the tactical question. From the United States point of view, what should we do if we face an institution that is obdurate and is not prepared to think broader in long-term arrangements? Maybe we have to tactically depart from GATT and from MFN sufficiently to bring a sense of reality to the broader institution.

In an ideal world, we would reform the GATT. I don't see that in the near future, or at least in a major way in the near future.

Senator BAUCUS. In exhibit 2 in your testimony you list the various, as I understand it, kinds of subsidies. Which subsidies do you think should be countervailed and which not?

Professor JACKSON. I sat down one weekend and typed the list. I think there were 56 on that list, and I'm sure you could go another couple of hundred; there are just so many different practices. What I do is, I throw that to my students, and I ask them this question that you asked me. [Laughter.]

There aren't too many of those on the list that I can give you an answer for. There are some that are obvious, an obvious grant of a government, a straight grant of a concessional loan or a concessional equity. It seems to me that when that has an effect across the border, then we should countervail. But remember the injury test. The injury test is more important than many people give it credit for. It is sort of a mediator between these conflicting policies of national sovereign goals and the international framework that we are trying to achieve.

Senator BAUCUS. So, you would look more at the injury test, then, as a major determiner?

Professor JACKSON. I could go on, but the bell rang, and I don't know what that is supposed to mean for me.

Senator BAUCUS. Well, it depends. [Laughter.]

The CHAIRMAN. It means that Senator Baucus is done, but you are not done.

Professor JACKSON. OK, fair enough.

When you go through, into the items on that list, there are some that are very intimately part of the culture and society. For example, you could argue that bankruptcy laws, in a sense, are a subsidy. And I think we should avoid countervailing in those kinds of things. That is why I would use this term "actionable subsidy" and try to define what kinds of subsidies we deem to be actionable. There are a variety of tests.

One test is the so-called specificity test or the general availability test. I am sure you have encountered that. And I am a proponent of that if it is not used too far. And there is some economic rationale for that: If you, in fact, are doing something that you could technically call a subsidy but it is available to all comers in society and is actually de facto available to all comers in society, such as accelerated depreciation in your Tax Code, it seems to me that we ought not to be countervailing that. For one reason, you can probably demonstrate that the effect across the border, at least in a floating exchange rate world, is very, very minimal indeed. So, that's an example of the kinds of things. I enunciate several different other principles.

A de minimis test should be important. We now have a 0.5 percent de minimis test that is applied by the Commerce Department. I suggest that is too low. That is going to involve foreign enterprises in a rather costly proceeding for very little importance; so I would at least prima facie consider raising that de minimis requirement, maybe with the possibility of a domestic interest demonstrating in a particular case why a lower de minimis is important.

Those are some of the things I suggest in my paper.

Senator BAUCUS. Thank you.

The CHAIRMAN. Professor Wallop? Senator Wallop—pardon me.

Senator WALLOP. I just got a promotion, I think. [Laughter.]

Professor JACKSON. You flatter me. [Laughter.]

Senator WALLOP. To begin with, I have an observation: That is, those who testified and said they were concerned about the low wages in other countries, by denying them access to these markets, do nothing but repress them even further. But they really don't do anything about raising income levels and standards of living in the countries in which they express so much concern.

But I am interested in having you flush out a little more this concept of interface, because it strikes me that as one observes the world's economy now it is undergoing a change that is every bit as major as the Industrial Revolution was. I don't think we understand all of what is happening, any more than people understood all of what was happening when that was taking place.

But when you see, for example, Japan now losing the steel production market to Korea, something different is happening out there.

And when you see the difficulty that we have in measuring trade, I think, when one examines figures and adds up all the countries of the world's trading figures, you find that the world has had something like a $20 billion deficit trading with itself. So, we are in the process of finding the means to define whatever it is that we are concerned about.

As you get into the interface of different cultures, where is an important beginning in trying to determine what is a cultural circumstance that is not likely to change and what is a cultural circumstance that could change?

Professor JACKSON. In a sense, I think we have made a beginning. I think the so-called unfair trade rules were kind of a stumbling beginning to this process. They really came to us out of almost a century of history, at times when these rules were not very important and these activities were not very important. But in the last several decades they have become very important, indeed, because of the falling of other barriers, including natural barriers—transportation costs and so on. So now we are seeing that they are very important, and I don't think we should be addicted to them in their current form.

Now, I think there are practices that governments are engaging in that are in a sense malicious, that is quite fair to call unfair. We should continue, perhaps, this regime to respond to those, but being a little more sophisticated and a little more flexible in evolving the regime so that we don't get stuck on rules that we defined 10 years ago that are really out of date today.

But another approach beyond that, particularly for these areas of sort of cultural differences, I think, is to have something that is more morally neutral, something where we get together with the foreign country and we say, "You've got your system; we've got our system. We both have legitimate reasons for our systems, but when they try to work together we are getting sparks instead of meshing."

So we have got to sit down together and figure out some kind of mechanism. Maybe it is some kind of buffer mechanism. Maybe, in fact, to a certain extent the antidumping program is doing some of this, but it is doing it in a very odd way and perhaps in an overly expensive way.

I guess I would think that we might open our mind to more sort of ad hoc arrangements. I do not like the ad hoc arrangements that are quantitative in result; but we might have more ad hoc sort of agreed arrangements at the price level, just saying that we do need a buffer for a variety of sound policy reasons—maybe there has to be a little price mechanism in there, a 5 percent or something like that, call it a duty if you want—but don't necessarily, in that phase, tie it to fair or unfair principles. Just say, "We've got a problem; we have got to solve it."

Senator WALLOP. That brings you down to something that you mentioned, sort of in passing, that, in addition to the round, we might be looking at more direct bilateral relationships—ourselves with Japan, ourselves with Germany, ourselves with Denmark—depending some on the product and some on the culture.

Professor JACKSON. Overall, I think the world is much better off if we can do this multilaterally. But there is such fundamental disagreement between our country and other countries and between other countries on some of these issues, so that sometimes the multilateral approach just can't achieve anything. At that point, I think, we could legitimately ask if we shouldn't move to a bilateral approach.

Senator WALLOP. There again, Mr. Chairman, and I would just close with this, it seems to me that is changing the culture faster than anything is the incredible speed with which information is available to people anywhere.

I have a friend in London who has a computer on his desk, from which he accesses something like 85 world markets; just by sitting at his desk, he has currency markets and commodity markets. It seems to me that that is going to change the culture faster than anything, because you can't stop it from affecting the way people behave and think.

The CHAIRMAN. Senator Bradley, then Senator Long.

Senator BRADLEY. Thank you very much, Mr. Chairman.

I would like to explore the issue of the existing trade laws that are supposed to respond to unfair trading practices abroad and be a deterrent to those practices.

In fact, what happens is that there is a great deal of Presidential discretion, and that, therefore, the issue becomes politicized immediately, and the very politicization of the issue prevents the unfair trade laws from being a deterrent to the imposition of unfair trade barriers abroad, in Japan and in the European Community, and in a variety of other places.

My question to you is, what changes would you recommend in the way those laws function in order to restore, or at least create, their deterrent value vis-a-vis countries like Japan and the European Community that do put up unfair foreign trade barriers with impugnity?

Professor JACKSON. With respect to the laws relating to imports into the United States, I gather you are really not referring to that. You are referring to our problem——

Senator BRADLEY. I am referring essentially to section 301.

Professor JACKSON. Yes. Part of the problem is, section 301 is extraordinarily broad, and it gives the United States a unilateral right of decision, which, I think, is appropriate in a national sovereign but that goes so far as to giving the President the authority to break international agreements when he thinks that is necessary. It also goes so far as to allow the President to seek redress from foreign countries for practices that are not inconsistent with any international agreement, and which in their view may be perfectly fair.

I don't claim to have thought this through entirely, but one possibility might be to more sharply divide the cases where there is already an international agreement on what the rule or norm is and we are going after somebody's violation of that, from other cases. That is already partly divided in 301, but we might sharply go a little further than that.

But underlying your question, really, is a very broad and perplexing issue of how much discretion the President should have in international economic relations generally.

I find myself torn on that, because in today's world a President seeks levers, he seeks bargaining chips on the world scene for broader geographical purposes. After all, our first goal is to preserve the peace.

In many cases the military option is essentially ruled out in today's world, more so than, I think, it was 50 years ago or what have you.

Where does he turn? Well, we have seen he turns to economics, he turns to economic chips. And I am not sure—every time you begin to limit his discretion, in a sense you are going to somewhat disable him from carrying out those broader tasks.

Senator BRADLEY. Well, if it is important to create a tool that is actually effective to pry open foreign markets, and if the present approach isn't working, then what kind of added clout would you provide? For example, I have toyed with the idea of tying access to foreign markets with a brief protective barrier against imports from that country to the United States in a specific sector, unless they open their market.

Professor JACKSON. Yes.

Senator BRADLEY. In other words, you tie 301 with 201.

Professor JACKSON. Oh, I see. I didn't see that last element.

Right now we are in the middle of a sort of minipasta war with the European Community. We have imposed some sanctions on the Europeans for reasons that we think are valid. We have a GATT panel, which has not yet been confirmed by the political processes, which rule in our favor. And yet, the Europeans found it in their interests to immediately counter-retaliate.

So, I am not very sanguine that this route is going to be very productive. I have a hunch that we are really involved in longer term persuasion, and I am not sure that we really have the clout that is going to help, at least in the short term, too much.

Senator BRADLEY. Thank you.

QUESTIONS FOR THE RECORD BY SENATOR BILL BRADLEY AND PROFESSOR JACKSON'S RESPONSES THERETO

Question. Would you agree that our trade laws, and particularly our laws intended to increase access to foreign markets protected by unfair trade barriers, are not deterring unfair foreign trading practices as intended? Is the deterrent power of our unfair trade laws strengthened or weakened by excessive Presidential discretion that politicizes every petition brought before the U.S. Trade Representative to improve market access? If over-politicization of market-access cases does indeed weaken the deterrent power of our unfair trade laws, what changes would you recommend to strengthen the ability of those laws to deter unfair foreign trading practices, and particularly those practices that restrict our exports?

Answer. I agree that U.S. trade laws are not completely successful in deterring foreign actions which discourage U.S. exports. Whether changes in those U.S. laws, particularly Section 301, could improve this deterrence I am unsure. Part of the problem is that the United States does not have as much relative economic power as it once did, so when dealing with certain trading partners (e.g. the EEC), U.S. pressures based on retaliatory activity do not have as much impact. In addition, on many issues there is a lack of agreement with our trading partners about what is "fair" or "unfair" behavior. U.S. pressures to change foreign practices about which there is such lack of agreement will almost always be relatively unsuccessful, since it engenders resentment and reactions to "foreign interference" with domestic affairs or policies.

I am dubious that tinkering with the U.S. President's discretion in these cases will have such effect on world trading practices. The solution, if there is any, is more likely to come through improved international institutional mechanisms allowing governments gradually to evolve rules that appear to all to be fair and evenly applied. This means, however, that the United States must be willing occasionally to bend its own views to accord with international agreement. The current configuration of U.S. law does not always allow this to happen. Thus foreign governments can argue that the United States is just as prepared to deviate from international rules as are certain foreign governments. This reduces the moral force of U.S. attempts to get compliance with those rules which it favors.

With respect to Section 301, I would more sharply distinguish the cases where the United States is proceeding against practices which are allegedly inconsistent with international agreements, and those which are not. Particularly in the former case, an international proceeding to determine noncompliance with the international rule is very helpful in promoting compliance if an efficient procedure exists for this purpose. This implies the need to greatly improve those international procedures.

With respect to activity on which there is not yet international agreement about its "fairness," we are essentially in a negotiating rather than a rule application mode. Thus the President will necessarily have to continue to excercise considerable discretion and ability to compromise. The original primary goal of Section 301 was to give U.S. officials the apparent authority to enable them through negotiations to achieve substantial (but not necessarily perfect) results on behalf of U.S. commercial and exporting interests. The goal was not to apply countermeasures, but to use the potential of such countermeasures for negotiating purposes.

Mr. Chairman, if I could—I am going to have to leave to go to another hearing—I wanted to just take the opportunity to welcome a member of the next panel to the committee.

The CHAIRMAN. Go right ahead.

Senator BRADLEY. It is Mr. Mike Aho, who served on my staff and was on the Finance Committee here for 2 years, and was instrumental in the writing of the report of seven people to the GATT. I was one of those seven people that Arthur Dunkle, the head of GATT, convened for a study of over 14 months. The report was issued last April, and it was really an expression of the GATT and a recognition that there are major problems with the GATT. I think that the committee would do well to probe him on not only the report but on his general views of what the next trade round could consist of.

I am unfortunately caught between Energy, Finance, and Intelligence, and I will have to see him at a later time.

The CHAIRMAN. It is a problem we all have, and we understand.

Senator BRADLEY. I thank Senator Long for yielding.

The CHAIRMAN. Senator Long.

Senator LONG. Professor Jackson, you started out by saying that you were not an economist, so that sort of puts us on the same level. I am a lawyer by profession, but I haven't practiced in so long that I am not sure I even qualify as a lawyer anymore. But I was once a lawyer, and I took a few courses in economics, so I know a little about it, and I have listened to economists talk now for about 36 years around here, long enough to know that a lot of them just have got to be wrong.

[Laughter.]

Senator Long. Your testimony makes me think about something that Mike Mansfield once said about lawyers. You know, Mike was not a lawyer, but he was a decent guy and a good college professor. Mike said that he didn't know anything about law, but he had observed this about law: That any case he had ever seen had lawyers on both sides—one side would win and the other side would lose. And from that he concluded that lawyers have to be right about 50 percent of the time.

I wonder whether economists are even right that often.

Now, if you go back a couple of hundred years, all that medical science would tell you was that if you were ill, the thing to do was to get yourself some leeches, and put those leeches on and have them suck some blood out, and that after a while you would feel better and get well. Now, what was so magical about those leeches nobody could tell you, but eventually you would apparently get well.

In the course of history, a couple of hundred years is just the bat of an eye, and I have found myself wondering whether advice we are getting now, at least what they are teaching in the great universities like Harvard and Stanford, might not rate alongside the advice that medical science was giving us a couple of hundred years ago.

Now, this much is fairly obvious to me, and I don't think the economists generally agree with it: If somebody is selling to me at a loss, and I keep buying from him especially if I am going into debt to but it—over a period of time I am going to go broke. I don't know what is going to happen to him, but I am not going to be very well off.

So, here we have a trading system that is being kept afloat by the United States running up about $150 billion worth of debts this year; in due course it will be a couple of hundred billion a year. At the rate we are going with the present system, we are advised that other countries are doing us a favor to sell at these cheap prices and make that labor available at low prices.

From what I not know about the free market system, if you do what the macroeconomists tell us we ought to do, we will have capital pursuing labor, or capital going wherever it can find the lowest cost to produce. So, for whatever reason—low labor costs or the fact that the local government does not have national defense costs or other practices that work out to be comparative advantages—the debt is bound to catch up with us.

Suppose this policy continues for 25 years—and that is only a short time in the history of mankind. I have served here for 36 years, and I don't think that is a very long time anymore. How much debt do you think we can run up to finance this trading system before the people find out and say, "We are not going to pay it" and before we won't be able to pay it or we will become a basket case just like so many other nations of the world?

Professor Jackson. Your series of questions are not easy to answer. I should point out that not only are economists wrong sometimes, but of course, as you say, lawyers. I suspect governments even are sometimes wrong.

I think you are putting your finger on something, though, that should be embellished here, and that is that we have got a very,

very significant macroeconomic problem. Apart from digging into the interstices of this or that unfair practice or this or that industry, we have got an enormous macro-problem. And when we have an exchange rate that will swing 20 or 30 percent in even a half-year, a 5-percent tariff or an 8-percent antidumping duty or what have you is just not very relevant.

I don't know the answer of how much debt we can incur. I am reading economists on both sides of that issue now. Some economists are arguing that what is said to be debt is not really debt, that there are different accounting principles that are involved.

I really can't answer the precise question you put; but in the broader context I think you have made a very good point: We have a very important macro-problem, the problem on the monetary side, that is imminently linked to the trade side, and we need solutions. I can't offer them.

Senator LONG. Could I just ask one further question, Mr. Chairman.

The CHAIRMAN. Yes.

Senator LONG. We used to run up enormous debts, that one American owed other Americans. However, now we are persuading other countries such as the Japanese, to let us owe it to them.

Now, with us running up these very large debts—$2 trillion on the gross national debt here, and give it 4 or 5 years and it will be a trillion dollars we'll owe the rest of the world—the debt will keep building at the rate of about a trillion dollars every 5 years unless we turn things around. That's a lot of money.

If we keep going that way very long, there is only one way that we will ever get out of that trap. We might just pay it. That's one reason I'm satisfied this Government won't go bankrupt. If we must pay it the Government can just say, "Well, look, if you are worried about being paid, we'll pay you. What do you want it in? Do you want it in $10 bills? Do you want it in $1,000 bills? Do you want it in $1 billion bills, or do you want it in $1 trillion dollar bills? We will do it however you want us to do it. Just give us a little time to put a few more numbers on those dollars down there at the Bureau of Printing, and we'll pay you." [Laughter.]

That is the kind of answer you begin to get into if you keep running up the debts the way we have been doing them. And I don't think we can keep doing this type of thing. It seems to me that at some point we will have to find a way to get back to what seemed to be the idea when I first came in, and that is to have a balance. What's wrong with having a balance of trade between ourselves and other nations?

Professor JACKSON. Most of the people I talk to, economists and businessmen and lawyers, and certainly some political statesman like yourself, say that the big question is the deficit of the U.S. Government expenditures. So that is where the finger points outside of Washington.

Senator LONG. Well, that is only because we haven't had a chance with that international debt very long. But it is going up very rapidly indeed now, isn't it?

Professor JACKSON. There is a connection. There is a connection.

Senator LONG. Well, thank you very much.

The CHAIRMAN. Senator Chafee?

Senator CHAFEE. Professor, we have testimony after testimony that it is this problem or that problem that causes the trade deficit of the United States: "Other countries are producing at a far lower cost because their wage rates are down; we are hobbled with our export controls; we don't have the tax system, the value-added tax; we have an income tax; there are not savings" and on it goes. But isn't it true that if we got this U.S. deficit—I mean our budget deficit—eliminated or on a downward path so that it was within the traditional limitations as a part of GNP, or whatever norm you wish to use, that this trade deficit would be vastly reduced?

Professor JACKSON. That is my belief and understanding, Senator. I do not speak to that from my own personal expertise, but the advice that I get certainly confirms your statement.

Senator CHAFEE. We have had testimony from both the former USTR, Ambassador Brock, and from the present USTR, Mr. Yeutter, that 60 percent of our export problems, and I believe that can be translated into import problems as well, are due to the value of the dollar—60 percent. And who can quantify it? But it may be more. Do you agree with that?

Professor JACKSON. That, again, is what I believe and what the advice I am getting says.

Senator CHAFEE. Now, let me ask you something else. We had testimony yesterday from the President of the United Auto Workers who said that they bargain for their workers for wages and fringe benefits. And true, it may be $25 per worker per hour, including fringes; but part of what they have to bargain for are the health costs, and in Canada the government pays for those health costs, so the company doesn't pay them.

You mentioned police and fire protection; should that be considered an unfair subsidy, along with low-cost power? In the end, somebody has to pay for those things in that country. Either the Canadian manufacturer is paying higher taxes so that the government can pay for the health insurance, so it can go for nothing to the workers. In some way it is paid for by the company, isn't it?

Professor JACKSON. I would think so. It has to be.

Senator CHAFEE. Therefore, why do we moan over these so-called "subsidies" that presumably have to be reimbursed in some way from the system? I don't know who pays it, but somebody other than the goverment really pays it. Is that true?

Professor JACKSON. I think when they are the kinds of practices you mentioned, that is, where they are generally available throughout the economy to all comers, then we should not respond to them under an "actionable subsidy" concept.

Senator CHAFEE. Do you mean if low-cost power is available to everybody?

Professor JACKSON. That's right. If it is available only to the steel industry, then it seems to me you have got another question.

Senator CHAFEE. I think that is a good differentiation that you have drawn. If France for example, is going to give a subsidy, an interest subsidy, or make it possible to give a low-cost loan to Indonesia if they will buy the Airbus, as opposed to buying a Boeing 763, then that is a targeted subsidy. Is that right?

Professor JACKSON. That is right.

Senator CHAFEE. So, I think what I'm getting at is, there is a way to differentiate between these subsidies that you pointed out so well in your testimony. Do you think we can arrive at those?

Professor JACKSON. I think we can gradually prick out a series of borderlines. I think we have begun doing that.

I think it is very important to have an institutional process that allows that to go on intelligently, and there are some questions about that internationally and nationally; but, nevertheless, I think I am reasonably optimistic that we can over time become more and more intelligent about this, both to balance the goal of avoiding too much intrusiveness on foreign government operations, but still trying to promote this system of world welfare that diminishes the distortions of particular subsidies.

Senator CHAFEE. Let me ask you a final question: If we got our deficit under control in this country, what would happen to the dollar? We all sit here and say, "Then the dollar will weaken," but we have also had some testimony that the influx of money into the United States isn't all for high interest rates, some of it is for a safe haven.

Now, it may also show that we are such a responsible government that we can run our affairs responsibly, and that makes the United States an even better place to invest, so the dollar would be strengthened. Can you see that happening?

Professor JACKSON. Yes, I have heard that.

Senator CHAFEE. That is no reason not to do it.

Professor JACKSON. I understand.

Senator CHAFEE. But do you think that might happen?

Professor JACKSON. I think it is certainly one of the possibilities. I guess my hunch is it is not a probability. But one thing that does appear to me as a layman economist—mind you, I am not an economist by training—is that the international monetary system and the exchange-rate system that is supposed to reequilibrate problems of disparities among countries has not been working, and the safe-haven phenomenon probably is one of those that has been affecting it. In certain ways it prevents it from working. There may be other factors, too. And I think that deserves close attention.

Senator CHAFEE. Thank you, Mr. Chairman. Let me just say I think the safe-haven factor is not based on any world mechanical system; it's just that "here is a better place to get a better return on your money." And it is going to be here 10 or 15 years, hopefully, in the future; whereas, other places present greater risks, political risks.

Thank you.

The CHAIRMAN. Any other questions?

Senator BAUCUS. There is one brief point I would point out. Professor Jackson, I don't know if you were here—I guess you were not—but the preceding witnesses from two very successful electronics firms, semiconductor industry firms, were basically saying that, although there are some unfair practices in the world, they are doing well because they just get up earlier in the morning and they just work harder, compete harder, are smarter, and they just do a good job, and they can cope with all of this nonsense that goes around.

Now, my question to you just at a gut level—you strike me as partly a lawyer, partly an economist, partly a lot of things—is how much of the trading problems we have today are due to the macroproblems, the dollar and so forth, how much are due to the unfairness problems, whether they are export controls or whatever, and how much is due to underlying competitiveness problems in this country?

Most people would confine our trading problems to those three areas. I just want to quantify the gut level. I mean, is it 33-33-33? Just where do you see the solution?

Professor JACKSON. Well, first I should say that I did hear a part of that testimony prior to mine, and I was very impressed; I thought it was very, very interesting and a far sighted approach that we were seeing represented.

I think I am willing to accept the advice I hear, that something around 50, maybe 60, percent is an exchange rate problem, a world disequilibrium problem, and that leaves the rest to be divided into these pieces that you have mentioned. My hunch is, the factor that you are talking about now—that is, U.S. competitiveness—is probably the single largest of that. The U.S., after all, has been privileged to be in a position for many decades of not facing too much in the way of world competition. We are moving into a new world now.

On the other hand, we see companies that are responding. The auto industry in my State seems to be responding very well, even though there are still complaints in that area.

Senator BAUCUS. So you think a large part of it is our underlying lack of competitiveness?

Professor JACKSON. I think a large part. I wouldn't put a percentage figure on it, because I just don't think that can——

Senator BAUCUS. That's all right. I agree with you. I think that is a fundamental problem.

Thank you.

The CHAIRMAN. I'll tell you, Max, an interesting story about a lumber company in Oregon—and I backed into this. It is run by a fellow named Adolph Hertrik. He is either German or Swiss. He had never been in the lumber business, and he came to the United States some time ago and opened a lumber company. He bought an old mill—it wasn't a particularly efficient mill—and he was convinced he could sell on the Japanese market. You know the complaints our people have about Japanese-sized standards and everything else? Well, he thought he could compete.

He lost money in 1978 and he lost money in 1979, and he lost a little in 1980, and he finally began to break in. And the Japanese want very high-quality finished lumber for post-and-beam interior construction.

I didn't learn about him until about 1982. What he had done, he had built himself a Japanese teahouse on his lumber company yard, so that when the Japanese buyers came he could show them the product.

The Internal Revenue Service had refused to allow this as a necessary cost of doing business, and he was attempting to explain that what he was trying to do, he thought it was a necessary cost of business.

I argued with the IRS, and they finally allowed it.

Well, this fellow now employes 70 or 80 people. He is selling about 80 percent of his output to Japan. The Japanese used to have an inspector there all the time, but they now take his inspection standards.

There is one person who has proved somehow that if you are willing to go about it—and this is somebody who came from no background in the lumber industry—if you are willing to go about it in a very methodical fashion, including building this teahouse with the post-and-beam construction for his customers to see, you could do it.

Most of my timber people are still complaining that they cannot sell on the Japanese market. Maybe this person is an anomaly, but he succeeds in doing it.

Professor **Jackson**. Thank you.

The **Chairman**. Thank you very much, Professor.

Professor **Jackson**. Thank you, Senators.

The **Chairman**. Now we will move on to a panel that very generously agreed to come back today: Mr. Hufbauer, Mr. Lawrence, and Mr. Aho. We had them scheduled for yesterday, and we had so many witnesses that we couldn't finish. I am very appreciative of their staying over.

Unless you have any objections, we will take you in the order in which you appear on the witness list, and take Professor Hufbauer first.

STATEMENT OF GARY C. HUFBAUER, WALLENBERG PROFESSOR OF INTERNATIONAL FINANCE, GEORGETOWN UNIVERSITY, WASHINGTON, DC

Professor **Hufbauer**. Thank you very much, Senator. I admire your stamina and your colleagues' stamina in listening to all these panels. I conclude that you must have really enjoyed your college classes.

My statement addresses two critical issues that have been touched upon by the other witnesses: First, what measures should have been taken both to reduce the U.S. trade deficit and to address the growth slump in the world economy? And second, what further policies should be adopted to answer unfair or injurious foreign trade practices that affect U.S import and export markets?

In my view, the U.S. trade deficit very largely reflects macroeconomic policy decisions taken since 1980. To try to respond to Senator Baucus's question on quantification, I would say that 85 to 90 percent of the trade deficit can be accounted for by macroeconomic policy, meaning, quite specifically, the overvalued dollar exchange rate and slow growth in the rest of the world.

If that diagnosis is correct, then I must conclude that the trade deficit should be answered through appropriate macroeconomic policies.

Now, if the world economy were purring along at a satisfactory growth rate, then macroeconomic policy could focus solely on correcting exchange rates. A very reliable econometric relation in the connection between exchange rates and trade balances. If everything were going along fine, policy makers could say, "Well, just get" the dollar down and the yen up, and that is the end of the story." But we have a world economy that is misfiring. Japan and the neighbors in the so-called "dynamic" Pacific region are slowing down, and the European economy has stalled completely.

Under these circumstances, if the United States suddenly discovered fiscal discipline—you might say that is not going to happen, so why worry?—but if we surprise ourselves with fiscal virtue, and if Japan proceeded to tighten money so as to strengthen the year, what would happen? The dollar/yen exchange rate would continue on its path towards more sensible levels, but I think the global economy could easily be pushed into a downward spiral. I conclude it is not enough to get the U.S. budget deficit down and Japanese interest rates up and leave it at that; we must also get foreign economies up. We must correct the trade imbalance through coordinated macroeconomic policies that lead to a more buoyant world economy, not to a world depression.

In today's circumstances of ambiguous administration leadership on global economic questions, I see ample room for Congress to point the way toward better policy coordination. As a modest start, I would suggest that Congress might ask the Congressional Budget Office to issue periodic "coordination reports" on the policies of the industrial giants.

Turning to another aspect of the macroeconomic picture, I think that Senator Bradley's proposal for a strategic currency reserve could provide a firm foundation for a new exchange-rate system.

Here, let me just briefly quote from something which came in the mail just yesterday from a Wall Street firm. This Wall Street firm says,

> We continue to wait to sell the deutchmark and other European currencies until when and if the deutchmark hits the $39.25 to $39.50 area. However, if this has not happened before Congress adjourns in December, we may go short at that point anyway, on the theory that the primary reason for the G-5 agreement was to blunt protectionist sentiment, and that a good time for corrections is when Congress is on an extended break.

In other words, we have some important players in the foreign exchange market who are just waiting to push the dollar up.

One final point. This committee might wish to link U.S. progress on deficit reduction to foreign progress on achieving faster growth.

To conclude: while trade imbalances primarily require macroeconomic solutions, I don't think that trade balances can be entirely divorced from trade policy. The linkage I have advocated before and I would advocate now is a strategy of "harnessing the wind." By that phrase I mean that the large trading countries should pledge themselves to liberalize their import restrictions, unilaterally and automatically, when they run persistent current account surpluses.

Let me stop there. Thank you.

QUESTIONS FOR THE RECORD BY SENATOR BILL BRADLEY TO PROFESSOR HUBBAUER AND HIS RESPONSES THERETO

Question. Would a managed floating exchange rate system better reflect the degree of economic interdependence in the world today than the current system of pure floating rates and illusory macroeconomic independence?

Answer. Yes. Under the present system of free-floating exchange rates, the entire burden or reconciling discordant macroeconomic policies among the major industrial countries falls on the exchange rate system and thus on the sectors of the economy that produce traded goods. This burden has caused such huge swings in exchange rates that some countries have been forced to reconsider their basic monetary and fiscal policies. A managed system of floating rates would prompt the same sort of reconsideration, but at a much earlier stage. As a result, the sectors that produce traded goods (about a quarter of total economic activity) would not be compelled to carry such a disproportionate share of the burden of reconciling macroeconomic policy differences.

Question. Can periodic, moderate intervention in international currency markets break currency speculation that artificially inflates the dollar and erodes the competitiveness of U.S. industries?

Answer. Much of the huge rise in the exchange value of the dollar between January 1983 and March 1985 can only be explained by currency speculation. By mid-1983, the dollar was clearly overvalued in terms of economic fundamentals. Yet it kept going up. In 1983 and 1984, I often said that a small dose of intervention would do wonders to take the hot air of speculation out of the system. The conventional answer—voiced by highly placed government officials—was that no practical amount of intervention could turn the irreversible tide of private markets. We now see that conventional wisdom was wrong. A small amount of intervention in March 1985, reinforced by a second dose of intervention in September 1985, has brought the artificially high dollar down some 13 percent on a trade-weighted basis. I have no doubt that moderate intervention in future years can break similar episodes of speculation.

Question. Do you believe that private capital markets are more likely to cooperate with government intervention if the markets believe that the intervention will not be sterilized by offsetting monetary policy?

Answer. Yes. A policy of unsterilized intervention would mean, for instance, that when the Bank of Japan sells dollar reserves to buy a given quantity of yen in the foreign exchange market (thereby pusinng up the value of the yen), the Bank would not simultaneously buy the same yen value of Japanese government bonds. If private financiers believe that the Bank of Japan will not offset the contraction in yen availability in the foreign exchange market with an equivalent expansion of yen availability in the domestic Japanese bond market, the financiers will correspondingly believe that intervention means (in this example) a smaller total supply of yen. Accordingly, the initial intervention will give private financiers more encouragement to follow the Bank of Japan and buy yen. In this way, private capital markets will reinforce public intervention.

I should add, however, that even sterilized intervention can exert a significant impact on exchange rates. Intervention following the Plaza Hotel Accord was largely sterilized, but it significantly altered expectations held by private capital markets as to the future direction of exchange rates. The outcome is history.

The CHAIRMAN. Thank you.

Mr. Lawrence.

[Professor Hufbauer's written testimony follows:]

THE TRADE DEFICIT AND TRADE POLICY

Statement by
Gary Clyde Hufbauer
Wallenberg Professor of International Finance
Georgetown University

before the

United States Senate
Committee on Finance

Hearings on

U.S. Trade Policy and Unfair Trade Practices
November 20, 1985

Hollis Kurman assisted in preparing this testimony.

My statement addresses two critical trade issues facing this Committee and the entire Congress.

First , what further measures should be taken both to reduce the U.S trade deficit and to address the growth slump in the world economy?

Second , what further policies should be adopted to answer unfair or injurious foreign trade practices that affect U.S. import and export markets?

The U.S. Trade Deficit

The U.S. trade deficit largely reflects macroeconomic policy decisions taken since 1980. Trade policy is decisive for the long-run evolution of the world economy but at best can make a secondary contribution to the trade deficit. By and large, the trade deficit must be corrected through appropriate macroeconomic policies.

Broadly, economic policies since 1980 have been designed to arrest runaway inflation, to curb social welfare programs, and, in the United States, to stimulate private activity through lower taxes. Many of those goals have been achieved. The time has now come to focus macroeconomic policy on two new challenges in the world economy: first, slow global growth in the face of high unemployment, idle industrial capacity, and weak commodity prices; and second, massive trade imbalances which reflect large currency misalignments.

If the world economy were purring along at a satisfactory rate, then macroeconomic policy could be focused on adjusting exchange rates and trade balances. But the world economy is misfiring: Japan and its neghbors in the "dynamic" Pacific Basin are slowing down, while Europe has stalled completely.

Under these circumstances, what might happen if, at the same time, the United States rediscovered fiscal discipline and Japan tightened monetary policy? The dollar/yen exchange rate might be restored to sensible levels, but the global economy could easily be pushed into a downward spiral. Trade imbalances must be corrected through macroeconomic policies that lead to a more buoyant world economy, not depression.

To repeat a familiar message, we need far better macroeconomic coordination among the industrial giants. In today's macroeconomic climate, sensible coordination means that Europe and Japan should decisively cut their taxes and promote investment, while the United States should pursue liberal monetary growth and gradually reduce its budget deficit.

Credit must be given where credit is due. In the Plaza Hotel Accord, Secretary Baker took a welcome lead in policy coordination. Events since September 1985 indicate that exchange rate intervention is far more effective than the naysayers would have us think.

Nevertheless, exchange rate intervention alone cannot correct world trade imbalances and global stagnation. To address such fundamental problems, other macroeconomic actions are also required. And, on this score, Secretary Baker's freedom of maneuver is constrained by an ideological flank in the Administration that thinks each nation can pursue its own vision of monetary and fiscal policy, and that market forces (meaning exchange rates and interest rates) will perform any necessary coordination.

In these circumstances, I see ample room for Congress to point the way toward better policy coordination. As a start, Congress might request periodic "coordination" reports from the Congressional Budget Office. Senator Bradley's proposal for a strategic currency reserve could provide a firm foundation for a new exchange rate system. In addition, this Committee may wish to link U.S. progress on deficit reduction to foreign progress on achieving faster economic growth.

Although trade imbalances largely require macroeconomic solutions, they cannot be entirely divorced from the formulation of trade policy. The linkage I prefer is one that "harnesses the wind" of trade surpluses to the cause of trade liberalization. In this approach, each of the major trading countries would pledge itself to liberalize, unilaterally and automatically , its import restrictions when that country runs a persistent current account surplus. The U.S. Trade Representative should seek such pledges in the process of launching a new round of trade negotations.

Unfair and injurious trade practices

Unfair and injurious trade practices of foreign countries must be divided into two distinct groups.

First , unfair or injurious practices that hurt U.S. companies in the domestic market by means of excessive import competition.

Second , unfair or injurious practices that hurt U.S. companies in foreign markets by restraining U.S. exports.

The United States already has extensive legal mechanisms to deal with unfair and injurious imports. These mechanisms could, of course, be improved. But the glaring weaknesses in the U.S. legal structure are on the export side.

The import side of trade policy . The United States has pioneered the development of statutes to answer subsidized imports (the countervailing duty law), dumped imports (the antidumping statute), and imports based on pirated patents or copyrights (Section 337). As with most legislation, these statutes need periodic revision to answer emerging problems. For example, problems posed by natural resource subsidies and non-market economies are addressed by pending legislation. On the whole, however, the U.S. apparatus against unfair imports is largely in place.

The greatest deficiency in the U.S. statutory framework on the import side concerns the response to *fair but injurious* trade. In the years ahead, as new Koreas and Brazils emerge in the international marketplace, we will be seeing many more imports of this kind. The United States needs a fresh approach to meet the changing realities of international competition. The approach I favor requires a double shift in emphasis: first, a shift from administrative discretion to a more judicialized system of providing escape clause relief and adjustment assistance; and second, a shift from non-tariff barriers (such as OMAs or VRAs) to tariffs and auctioned quotas as a means of providing both temporary trade relief and revenue to fund adjustment programs. The Moynihan-Roth bill and other Congressional initiatives make a welcome start in bringing about both changes of emphasis.

Escape clause relief should be more readily available to impacted industries. In order to make this transition, two changes are essential. First, the causation standard that qualifies an industry for relief should be less stringent than the present "substantial cause" test. Second, once the International Trade Commission determines that an industry is injured by imports, Presidential discretion should be limited to the *form* and the *means of finance* of relief, not to the *existence* of relief.

Ideally, all new escape clause protection should take the form of tariffs or auctioned quotas. The revenues generated by temporary trade protection should then be dedicated to the long-term adjustment of the impacted domestic industries. Adjustment requires much larger retraining, relocation, and early retirement programs than we now have on the statute books. However, according to my calculations, tariff and auctioned quota revenues would be entirely adequate to fund worthwhile adjustment programs.

The export side of trade policy . How will the United States address the host of practices that keep U.S. firms out of foreign markets? This is the central question for U.S. trade policy in 1985.

Our leading export promotion institution for many decades has been the Export-Import Bank. But the Eximbank has never had sufficient resources to support more than about 10 to 12 percent of U.S. exports. It seems unlikely that this level of funding will expand much in the years ahead. Moreover, even an expanded Eximbank would not be a useful tool for overcoming many kinds of trade barriers. For example, a larger Eximbank could do very little to overcome Nippon Telephone and Telegraph's restrictive procurement practices.

In order to make headway in opening foreign markets, our laws must be rewritten to accomplish two things: first, to provide more automatic relief to exporting firms that encounter unfair and injurious barriers; second, to provide a remedy that can effectively open markets abroad, at the smallest possible expense to U.S. taxpayers or consumers.

In order to provide more automatic relief for export industries, the fact-finding work contemplated in Section 301 cases should be assigned to the International Trade Commission. If the ITC found a foreign practice that violated international agreements, then the U.S. Trade Representative should be required to take remedial action. If instead the ITC found a practice that violated no international agreement, but which nevertheless unreasonably injured U.S. export prospects, then remedial action would remain a discretionary matter with the U.S. Trade Representative.

If diplomatic representations by the USTR did not persuade the foreign country to reduce its barriers, what sort of remedial action would be most appropriate? The present approach of allowing the Administration wide latitude in selecting means of retaliation has not worked well. Countless bureaucratic hours are consumed in devising a retaliatory weapon; yet, as often as not, it misfires. At the same time, we must be wary of retaliatory measures that are biassed toward closing U.S. markets rather than opening foreign markets. For example, when retaliatory measures are aimed at protecting a specific sector of the U.S. economy, an unwholesome incentive is created for the domestic industry to design a nominal "market-opening" strategy that ultimately seeks the benefits of retaliation.

I would recommend a single remedy to deal with a wide variety of foreign market barriers. This single remedy would have the United States levy a low-rate tariff on all its imports from the recalcitrant partner country, and then dedicate the proceeds either to overcoming the barrier in the partner country's market or to promoting U.S. exports in third-country markets. A low-rate tariff imposed across the board would practically eliminate the benefit to any one industry from protecting the U.S. market and would focus attention on the real issue -- closed foreign markets. Moreover, it would provide revenue for meaningful relief if the foreign country refused to reduce its barriers.

Conclusion

The United States needs a triple strategy to deal with its three main trade problems -- trade deficits; unfair and injurious import practices; and unfair and injurious export restraints. Many elements of this strategy seem to be included in the new bipartisan trade bill previewed in the *Washington Post* on Saturday, November 16. With appropriate tailoring, I believe a bill can be fashioned that encourages both the Reagan Administration and our key trading partners to design a growth-oriented, fair international economic system.

STATEMENT OF ROBERT Z. LAWRENCE, SENIOR FELLOW, ECONOMIC STUDIES PROGRAM, BROOKINGS INSTITUTION, WASHINGTON, DC

Mr. LAWRENCE. Mr. Chairman, in other testimony this committee has heard that unfair foreign practices in the form of subsidies to firms and protective barriers on U.S. exports are the major source of current competitive difficulties for U.S. firms. It has also been alleged that these practices have seriously impaired the U.S. manufacturing base, and that without American retaliation, these practices could turn this country into a Nation of hamburger stands with low-paying services jobs.

In the first part of my testimony, I present evidence which suggests that these views are seriously inaccurate.

In arguing a minor role for unfair foreign practices in the erosion of our trade deficit, I make three points:

First, the allegedly unlevel nature of that playing field of international competition by U.S. firms in the 1970's, when our exchange rate stood at a realistic level. As recently as 1980, the United States had a surplus of trade in manufactured goods of about $18 billion.

Second, the recent trade balance decline is pervasive; it extends across all major product categories, and occurs with all of our major trading partners. If unfair practices constituted a major cause of the recent trade balance decline, we would be experiencing that decline only in certain product categories and with certain trading partners.

And third, I would estimate, using econometric techniques, that three factors account for over 90 percent of the trade balance decline: the relatively high prices of U.S. products account for about 70 percent, and the Latin American debt crisis and slow foreign growth account for the remainder. Without these developments, our manufactured goods trade balance would be in surplus today.

I also present evidence which suggests that the trend toward a services economy has been widely misunderstood. The share of the U.S. labor force employed in goods has declined over time primarily because productivity growth has increased more rapidly in goods production. Just as we reduced our workforce on the farms without reducing our ability to produce food, so have we reduced the share of employment in goods production without reducing our ability to produce those goods.

In 1960, goods production accounted for about 45 percent of total output in the U.S. economy. In 1985, it accounted for about 46 percent. Since the 1979 peak, employment in services has increased much more than employment in goods; yet, this again reflected productivity growth differences rather than output growth.

Although many goods-producing firms have experienced difficulties because of international competition, it is striking that between 1979 and the third quarter of 1985 our production of manufactured goods increased by exactly the same 14 percent as our production of services.

In my testimony I will present evidence which refutes the notion that a declining share of goods production will lead to a two-tier economy. Jobs in goods production provide about the same share of middle earnings income opportunities as jobs in the rest of the economy.

The second part of my testimony deals with policy options. Unfair practices, I agree, should be a focus of current trade policy. But perhaps even more important are policies to reduce the U.S. Government deficit, to stimulate productivity improvements, and to help firms and workers dislocated as a result of international competition.

First and foremost, our trade deficit reflects a Nation which has to borrow from the rest of the world because its Government has to borrow more than its private citizens are prepared to lend. No program of quotas or protection will change the unpleasant fact that this Nation spends more than its income.

Only with an installment program to reduce the Federal Government budget deficit will we remove the root cause of the trade deficit.

Beyond changing our fiscal policies, our trade policies leave tremendous scope for improvement. To aid dislocated workers, our 201 legislation and our trade adjustment assistance programs have to be improved.

In addition, I feel that we must deal with the problems making the playing field of international competition more level through international and bilateral negotiations.

Mr. Chairman, I will be happy to discuss my views on these and other aspects of trade policy in response to questions.

Thank you.

The Chairman. Mr. Aho.

[Mr. Lawrence's written testimony follows:]

Statement of Robert Z. Lawrence
Senior Fellow, The Brookings Institution
before the
Subcommittee on International Trade
Committee on Finance
U.S. Senate
November 20, 1985

SUMMARY

Unfair foreign trading practices are not a major factor in the erosion of the U.S. trade balance over the past four years nor are they responsible for the declining share of U.S. employment in goods production. Whereas the trade balance decline is caused principally by the strength of the U.S. dollar, the declining share of employment in goods production results from the relatively more rapid productivity growth in this sector. The dollar, in turn, reflects the large net capital inflows which have been required to meet the borrowing needs created by the large U.S. government deficits. The removal of protective barriers against U.S. firms abroad, while desireable in its own right, is unlikely to have a major impact on the overall U.S. trade balance. Nor would the adoption of protectionist measures in the United States influence the trade balance. Only measures which affect national spending behavior can achieve improvements in the trade balance over the long run. Among such measures, the most effective would be a reduction in the U.S. government deficit through expenditure cuts and revenue increases.

U.S. trade policies could be improved in several respects. There is scope for removing barriers to U.S. firms abroad and for reducing U.S. barriers at home. However, these actions alone will not improve U.S. trade performance. Policies which increase U.S. productivity and technological innovation and which facilitate the adjustment of firms and workers to structural change are also required.

Statement of Robert Z. Lawrence*
Senior Fellow, The Brookings Institution
before the
Subcommittee on International Trade
Committee on Finance
U.S. Senate
November 20, 1985

Between 1980 and 1984, the United States balance of trade declined by $87 billion. With the exception of the fuel trade with the OPEC nations, the slump has provided almost every category, present across all commodity groups and with all major trading partners. Bilateral deficits increased with the European Community (by 29.6 billion), Japan (by 24.1 billion) the East Asian NICs (by 17.3 billion), Latin America (by 16.8 billion) and Canada (by 13.8 billion). The red ink grew in trade in agricultural products (-6.2 billion), manufactured products (-98.1 billion), high-tech goods (-20.3 bilion) and low-tech goods (-77.9 billion), consumer goods (-30.7 billion), capital goods (-29.9 billion), and automotive products (-23.2 billion).

Many observers place a major part of the blame for these trade deficits on the policies of foreign governments. According to these observers, both protection of home markets and targeted subsidies for export industries have enabled foreign competitors to inhibit severely the ability of U.S. firms to compete in international trade. Some observers go even further to argue that unless the United States acts to offset these measures with similar aid to its own firms, its industrial base will be destroyed. The United States will be reduced to a second-rate power, able only to employ its workers in fast food stores and other low-paying activities.

---

*The views expressed in this statement are the sole responsibility of the author and do not purport to represent those of the Brookings Institution, its officers, trustees, or other staff members.

In this testimony I will argue that these views are profoundly mistaken. Foreign unfair trading practices have little to do with the dramatic erosion in the U.S. trade deficit. Nor do shifts in these practices have a major impact on the overall trade deficit. Trade deficits, a reflection of national spending patterns, is principally a response to U.S. fiscal policies. To reduce that deficit, spending patterns should be changed.

I will also suggest that it is inappropriate to adopt protectionist policies in an effort to prevent the perceived erosion of middle-class employment opportunities in the United States. The growing share of employment in high-tech and services industries will not significantly reduce the middle class. Regardless of shifts in U.S. international trade performance, the share of employment in the U.S. manufacturing sector is likely to decline. This reflects measures which improve U.S. living standards rather than lower them and should be facilitated rather than resisted. Finally, I will argue that counteracting unfair trade should not be the only or even the primary focus of U.S. trade policy. While improving the rules of international competition should comprise one element of trade policy, we should emphasize policies for assisting workers dislocated as a result of trade and for improving our own competitive performance.

Section I. Evidence

Can America Compete in an Unfair World? Evidence from the 1970s

Recall that between 1973 and 1980 the world trading system had the same features that allegedly prevent the U.S. from competing today. Surging competition was being felt from the Asian Newly Industrializing Countries (NICs) and Japan, and the European economies had already increased their non-tariff barriers and industrial subsidies by considerable amounts. Despite these measures, U.S. firms were able to compete with considerable success.

Between 1970 and 1980, the U.S. trade balance in manufactured goods increased from 3.437 billion to 18.8 billion or from 0.3 percent of GNP to 0.7 percent of GNP. The volume of U.S. manufactured goods exports increased by 101.2 percent, while the volume of imports increased 72.0 percent. Over this period, I have estimated that the jobs in U.S. manufacturing due to exports were virtually identical to the jobs that might have been gained had manufactured imports been replaced by U.S. products.[1] Between 1973 and 1980, trade had a markedly positive impact on manufacturing employment, adding about 280,000 jobs in manufacturing. These employment gains were widely diffused; jobs due to increased exports outweighed those lost to higher imports in 40 out of 52 U.S. manufacturing industries. Over this period, the declining trend in the U.S. share of world manufactured goods exports was arrested. The share was 16.4 percent in 1973, 16.4 percent in 1980 (and 18.1 percent in 1981). Thus over the 1970s, U.S. manufacturers competed relatively successfully in international trade.

---

[1] See Robert Z. Lawrence, "Is Trade Deindustrializing America: A Medium Term Perspective," Brookings Papers on Economic Activity, 1983:1.

Since 1980 the trade balance has experienced a substantial decline. But there is little room to include an increase in unfair foreign trade practices as part of the explanation for the decline in the U.S. trade balance.

If unfair foreign trade practices constituted a major source of the trade deficit, one would expect it to be concentrated in a few product categories and in only a few of our trading relationships. The pervasiveness of the slump suggests these practices are not to blame.

The declining trade balance is no mystery. Econometric evidence suggests that the declines in U.S. price competitiveness account for about $71 billion of the $98 billion decline in the U.S. manufactured goods trade balance between 1980 and 1984. Had U.S. manufactured exports to Latin America increased as rapidly as to the rest of the world, they would have been $8.6 billion higher in 1984. A further $8 billion decline in the balance can be ascribed to relatively weak growth abroad. In sum, these three factors explain 90 percent of the decline in the manufactured goods trade balance. The dollar's strength, and not unfair foreign practices, provides the proximate explanation for American trade performance. And the dollar's strength is in turn directly linked to the high real interest rates, which have attracted funds to the United States, primarily to finance the large government budget deficit.

The Shift to Services and the Middle Class

The stylized image of structural change in the United States is represented by the displaced steel or automobile worker forced to take a menial job in fast foods or electronic assembly. This picture has sounded alarm bells and produced dire forecasts about the future of th middle class. Even sophisticated analysts believe that, as the economy shifts away from basic manufacturing and toward high-technology and service industries, the number of mid-level jobs will decline.

Commentators have advocated protectionist trade measures and selective industrial policies to prop up basic manufacturing and to forestall the structural economic changes that they see threatening the middle class.

But neither these presumptions nor prescriptions are correct. One cannot get an accurate picture of structural change by looking at just a few sectors or relying on anecdotal evidence. The auto and steel industries have received a lot of attention, but even at their 1979 peaks, they accounted for only 1.1 percent of total employment.

Data on sectoral earnings tell a different story. In the accompanying table, the usual weekly earnings of full time workers in 1983 have been grouped by sector and divided into three classes.[2] Middle-class earnings are defined with reference to earnings of the median male ($379 a week or $19,708 a year). Jobs paying plus or minus a third of this level are considered to be middle-class.

Contrary to the common perception, the proportion of full-time workers with middle-class earnings in the production of goods is exactly the same as the proportion of workers with middle-class earnings in the rest of the economy -- 46 percent. Durable-goods manufacturing does rank second among all sectors in the proportion of its workers receiving middle-class earnings (50 percent). However, the public sector has the most intensively middle-class work force (55 percent), and in third place is the services sector: transportation, communications and public utilities (49 percent). There is virtually no difference between the proportions of middle-class earnings in nondurable manufacturing (44 percent), finance (43 percent) and miscellaneous services (43 percent).

Manufacturing may provide a larger share of middle-class jobs than the rest of the economy. But it scarcely represents the backbone of the middle class. If all manufacturing workers were to be re-employed

---

[2] For a more complete analysis see Robert Z. Lawrence, "Sectoral Shifts and the Middle Class," Brookings Review, Fall 1984, pp. 3-11.

Table 1. Earnings Distribution across Sectors, Categorized by High, Middle and Low Earnings, 1969, 1983[a]

Percent

	Distribution in 1969								
	Total			Males			Females		
Sector	High	Mid	Low	High	Mid	Low	High	Mid	Low
Total	20	50	30	28	56	16	5	39	56
Goods producing	21	53	26	26	58	16	2	38	60
Agriculture	5	25	70	6	26	68	0	16	84
Mining	32	52	15	35	52	13	1	56	44
Construction	32	50	18	33	49	17	5	57	38
Manufacturing	20	55	25	26	62	13	2	38	60
Durables	22	60	18	27	62	11	3	49	48
Nondurables	15	49	36	23	60	17	2	28	71
Services	17	45	38	27	54	19	3	33	64
Transportation, communication, and public utilities	23	61	16	28	62	10	4	55	41
Trade	15	43	41	23	54	23	2	25	74
Finance, insurance, and real estate	22	45	33	40	48	12	4	42	54
Private households	2	9	89	5	26	70	2	7	92
Miscellaneous services	15	42	43	28	49	23	4	37	59
Public sector	24	56	20	34	56	10	12	56	32

	Distribution in 1983								
	Total			Males			Females		
Sector	High	Mid	Low	High	Mid	Low	High	Mid	Low
Total	21	46	33	30	47	23	7	44	49
Goods producing	24	46	30	30	48	22	6	42	52
Agriculture	3	27	69	4	28	68	1	21	78
Mining	48	42	9	53	40	8	28	55	16
Construction	28	45	27	30	45	25	6	51	42
Manufacturing	23	48	29	31	51	18	6	41	53
Durables	26	50	24	32	51	17	7	49	44
Nondurables	19	44	37	28	51	21	5	34	61
Services	19	42	40	30	43	27	6	40	54
Transportation, communication, and public utilities	36	49	15	43	45	12	14	58	27
Trade	14	38	48	21	44	35	3	28	69
Finance, insurance, and real estate	22	43	35	44	39	18	7	46	46
Private households	2	8	90	2	18	80	1	7	92
Miscellaneous services	16	43	41	28	41	31	7	44	49
Public sector	23	55	23	32	53	15	12	56	32

Source: Bureau of Labor Statistics, unpublished data, Usual Weekly Earnings of Employed Full-Time Wage and Salary Workers, 1969, 1983.

a. Income categories established using median male weekly earnings of $142 in 1969 and $379 in 1983 as a middle benchmark. The categories are defined as follows:

high (1983) = $500+
mid (1983) = $250–499
low (1983) = $0–249

high (1969) = $187+
mid (1969) = $94–187
low (1969) = $0–93

with earnings patterns typical of the rest of the economy, the aggregate distribution of earnings would change very little. The number of workers receiving upper-class and middle-class earnings would decline by only 3 percent and 1.7 percent, respectively.

A similar analysis with a slightly different data base refutes the contention that the high-technology industries offer relatively few middle-class job opportunities. The proportion of middle- and upper-class jobs for both males and females is higher in high-tech than in the rest of manufacturing. All of the major high-technology industires (chemicals, electrical and non-electrical machinery, aircraft and instruments) have smaller shares of lower-class jobs than the rest of manufacturing and almost all of them have larger shares of upper-class jobs. The overwhelming source of the shift in employment to services economy is the relatively more rapid growth in productivity in goods production. The shift is thus a sign of greater prosperity rather than the reverse. Increases in services production have not come at the expense of goods production. Measured in 1972 dollars, U.S. goods output was 45.6 percent of GNP in 1960, 45.8 percent in 1979, and 46 percent in 1984. Just as rising farm productivity increased food production while freeing farm labor for employment in the factories, relatively rapid growth in manufacturing productivity is increasing goods production while making a larger share of the labor force available for employment in services. Despite the pressures from international competition over this recovery, it is striking that

American goods production has increased as rapidly as the production of services. In the third quarter of 1985, for example, the total U.S. output of manufactured goods was 14 percent higher than its 1979 peak. Overall U.S. GNP had increased by exactly the same percentage.

The United States is already a services economy. Only 25 percent of the workforce today produce goods. This shift has progressed so far that to understand the implications we have only to look around us. The advent of this expansion reflects advances in technology and productivity that enable us to meet the demand patterns of a high-income population. Public policy should not try to hinder this transition, but it may try to aid those displaced.

Section II. Principles

In principle, trade protection in the United States is not an appropriate remedy for our large trade deficits. To deal with these deficits, we must change U.S. spending patterns. To appreciate the connection between the trade deficit and the government budget deficit, it is useful to recall that the trade balance in goods and services is by definition equal to the difference between what the nation produces (its national income and output) and what it spends. If the trade balance is in surplus, for example, national production exceeds national expenditure of goods and services -- in other words, we export more than we import. If the trade balance is in surplus it also means that the nation as a whole is lending to the rest of the world; if it is in deficit, the nation is borrowing from the rest of the world. The nation's borrowing in turn reflects the borrowing of its private sector and the borrowing of its government. Since 1981 the U.S. has embarked on a course which will give it a large budget deficit at full employment. If the government increases its borrowing levels at full employment, either the private sector must reduce its borrowing (and be prepared to lend to the government) or the nation must borrow from abroad.

If government spending is raised in a fully employed economy, domestic residents will either change their spending behavior and purchase fewer goods and services, or they will have to purchase more imported goods and services. With changes in tax and spending policies, the United States government since 1981 has raised the federal deficit the economy will run in 1989 to an estimated $200 billion. In the absence of a corresponding decline in private spending on consumption or investment, this government deficit will have to be financed from abroad. U.S. national spending will rise relative to U.S. incomes, and via the trade deficit, the increased American demand for goods will be met from abroad. If government spending is raised without a change in the spending of private domestic residents, an excess demand for domestic goods and services may result. Eventually, however, the prices of domestic goods and services would increase relative to foreign goods, until domestic residents were willing to purchase foreign goods instead. A relative rise in the prices of U.S. products, manifested by a stronger dollar could in part facilitate this process.

In sum, the growth of the U.S. trade deficit is principally a response to U.S. fiscal policies. It is neither the result of an aberration in the exchange rate system, nor of a sudden surge in unfair trade practices. To the contrary, the emergence of the large current account deficit, driven mainly by changes in the relative prices of U.S. products, is evidence that the exhange rate responds to bring international trade flows in line with changes in national spending patterns.

How should the United States respond to the current trade deficit? In my view, no substitute exists for an installment program which would bring the government deficit into balance by both reducing spending and raising revenue.

Some argue that adopting protectionist measures of our own or dealing with protection abroad will improve our trade balance. I believe that these measures are unlikely to improve our trade balance. Just as squeezing a balloon will redistribute, but not reduce, the total amount of air in the balloon, so, in the absence of a shift in national spending patterns, will imposing tariffs and quotas only change the composition of trade, but not affect the overall current account deficit. Since the trade deficit reflects an aggregate excess of national spending over national income, spending less on one type of foreign good will simply mean spending more on others. Less imports of one good will therefore mean a combination of more imports of other goods, and less exports. The exchange rate is again one mechanism by which this process operates. In the short run, a quota could reduce imports, but it would also increase the current account, strengthen the currency, and thereby make it more difficult for other sectors in the economy to compete internationally.

Given national spending patterns, policies which promote the international competitiveness of one type of product in any economy will increase the competitive difficulties of others. Thus, for example, protecting industries like steel and textiles will, by keeping the dollar strong, hurt sectors such as computers and aircraft.

Many believe protectionist measures are an important source of the difficulties foreigners face in selling in Japanese markets. They advocate pressuring Japan to increase imports. If increased efficiency of world resource use is the objective, this strategy has merit. However, a more open Japanese economy does not necessarily imply a change in the Japanese trade surplus. Japanese current account surpluses ultimately reflect Japanese spending patterns. Given any level of Japanese income, production, and particular spending patterns, increasing Japanese imports will reduce domestic spending on Japanese products. In the short run, therefore, there will be an excess supply of Japanese goods. In order to sell them abroad, Japanese manufacturers may have to lower their prices. Thus, more Japanese exports will accompany the rise in Japanese imports. (The exchange rate may play a role in stimulating greater exports.) If Japan opens its markets, either the world will have to absorb more Japanese exports, or the Japanese will have to change their spending patterns. Increased Japanese demand for imports many mean a weaker yen and thus increased Japanese exports. In concrete terms, therefore, a policy of opening the Japanese market will probably mean greater competitive pressures for industries such as automobile and steel, in which the Japanese are highly competitive, in international markets. Conversely, placing quotas on Japanese exports to the United States of these products over the long run will mean more Japanese exports of other goods.

In summary, therefore, recognizing that current account deficits reflect national spending patterns has important policy implications. If particular deficits are seen as undesirable, shifts in policies which affect national spending patterns should be used. To lower a current account deficit, government revenues should be raised, government spending reduced, and/or private consumption and/or investment lowered. In the absence of a change in spending patterns, more imports will eventually lead to more exports or vice-versa. Sectoral policies (in the name of making trade more fair or not), such as tariffs, quotas and selective export credits will change the composition of trade and terms of trade. Over the long run, however, since these policies are unlikely to shift national spending patterns, they will leave the overall trade balance in goods and services unaffected.

Section III. Policy Options

Public concern is growing among both politicians and economists about the long-range implications of the current trade imbalance. Last spring, the U.S. became a net debtor nation for the first time since 1914, largely as a result of record borrowing from foreign creditors who help to finance the growing trade deficit. Continued increases in debt owed to foreign nations will ultimately be paid by sacrifices in future living standards, through shipments to foreign purchasers of U.S.-produced goods that American consumers would otherwise enjoy. If this debt repayment occurs through a substantial depreciation of the dollar -- which many economists believe is inevitable -- the cost of imported goods will climb and the rate of inflation will increase.

Erecting trade barriers here, either as bargaining chips or as purely protectionist devices, would only make matters worse. Added trade restrictions would only strengthen the dollar and reduce the competitiveness of American-produced goods in world markets. In addition, a turn toward protectionism by the U.S. could trigger retaliation by other countries, leaving all trading nations worse off, as occurred in the 1930s after the U.S. passed the infamous Smoot-Hawley Tariff Act. Finally, curtailing imports from countries now heavily in debt, such as Brazil and South Korea, could strain the American banks to whom this debt is owed and could threaten the viability of an already fragile financial system.

Many of the new advocates for protection in Congress recognize its dangers, but nevertheless voice their reluctant support for protectionist measures to close the worsening trade gap. Some cynics argue that lawmakers use the growing trade deficit to make foreign countries the scapegoats for the recent hiatus in the U.S. economic recovery. A more compelling explanation is that lashing out at foreign trade barriers can be more attractive politically than tackling the complex and divisive task of reducing the principal cause of the current trade imbalance -- the federal budget deficit, which most forecasters outside the Administration project may exceed $200 billion annually through the end of the decade.

In such an environment, repeated calls by economists, the news media and other opinion leaders for budget discipline as a means of paring the trade deficit are likely to fall on the deaf ears of lawmakers, who are pressured continually by workers and firms in trade-sensitive sectors of the economy battered by the strong dollar. (To be sure, the dollar has weakened somewhat in the wake of the Treasury Department's recently announced commitment to intervene with the finance ministries of Japan, England, France and West Germany in foreign exchange markets. In addition, some of the political momentum behind protectionism abated following the Administration's announcement of its intention to step up its enforcement of the laws against unfair trade practices.) Nevertheless, the political impulses to embrace protectionist remedies remain strong. They will only continue to push the Administration away from policies favoring freer trade; even more dangerously, they could result in concrete protectionist actions should U.S. economic growth continue to stall or the economy slide into recession.

Dealing with Dislocation

A far more productive course for lawmakers who are concerned about the dangers of protectionist remedies, but who nevertheless believe they have no other available options, is to design and implement effective policies for easing the dislocations induced by trade. Politicians continue to face political pressures for protection from firms, workers, and local communities adversely affected by import competition; lawmakers can and will find it difficult to resist calls for trade barriers if they cannot point to the presence of effective policies for easing the economic pain caused by changes in trade patterns. Put in economic terms, aid for trade-injured parties can both reduce the demands for protection and the willingness of elected leaders to supply it.

The U.S. has attempted in the past to provide such assistance, but with mixed success. I believe that the nation can do better, but only if government programs designed to ease trade-related dislocations are fashioned to promote, rather than delay, adjustment to change. The cruelest form of aid is that which temporarily salves an economic wound, but which, in the end, leaves recipients in an even worse position to deal with the harsh competitive realities of the global marketplace. This danger can be reduced if trade assistance programs conform to the following criteria:

-- Assistance must be temporary so that it does not encourage dependence.

-- Assistance must be transparent so that voters and politicians are aware of its costs.

-- Assistance must complement, rather than replace, market forces.

In a paper drafted by me and my colleague, Robert E. Litan, shortly to published by the Brookings Institution, we present several detailed proposals based on these criteria for easing trade-induced dislocations suffered by firms, workers and communities.[3] In part, our suggestions envision a fundamental redirection of two programs already in place -- the temporary protection available through the current U.S. "escape clause" law and the assistance provided to some workers under the trade adjustment assistance program. For firms and workers under our proposals, the starting point would be a determination by the International Trade Commission (ITC) that an industry is suffering from serious injury on account of import competition. The ITC determination would trigger two basic programs to ease trade dislocations in the industry. First, firms in the industry would be eligible for temporary protection from imports in the form of tariffs, but not quotas. Mergers of such firms would be judged under relaxed antitrust standards. Second, workers in the industry would be eligible automatically for compensation payments geared to their losses in income and for retraining loans, with repayments based on future income and collected through the income tax system.

---

[3] Robert Z. Lawrence and Robert E. Litan, "Living with the Trade Deficit: Adjustment Strategies to Preserve Free Trade," Brookings Review (forthcoming). Copies are available from the authors upon request.

Improving Performance

Over the long run, enhanced productivity and innovation are the keys to U.S. competitive performance, and should be the major focus of U.S. trade policies. On the positive side, efforts should be redoubled to improve the United States educational and training systems and to encourage the development of commercially viable technologies. In addition, barriers imposed by the U.S. government in the form of various regulatory constraints should be examined and relaxed.[4]

Dealing With Unfair Trade: Policy Options

Although it is not the principle reason for the current difficulties facing U.S. firms in international trade, reforming the rules of the game remains a major problem for U.S. trade policy. The world appears to act unfairly toward U.S. firms. Firms in other countries do receive more government assistance than those in the United States. There is the danger that a failure to respond could result in a global system even more shackled with protectionist measures. How should the United States respond? In dealing with these problems, we should keep in mind a number of factors. We must recognized that international trade will never be fair in the same way that domestic trade is fair. Fair competition between domestic firms is possible because they all operate in the same environment, and therefore their fate is determined by their own actions rather than by those of their government. Yet international trade occurs precisely because firms have access to different environments. Environments differ because of basic endowments, such as natural resources and climate. But they also differ because of social conditions such as political systems, laws, and degree of government support given to firms. Too often we hear that because governments can influence, or even create comparative advantage, trade theory is irrelevant to the real world. Yet, taking intervention as given, the principle of comparative advantage and arguments about the potential gains from trade remain perfectly valid. In a pluralistic world, nations need to accept the existence of different economic systems. They cannot confine trade only to systems similar to their own. When the United States trades with the Soviet Union, to take the most extreme example, what does fair trade mean? Yet they do (and should) trade with each other because both nations gain. Although the playing field of international competition can never be level, therefore, we can obtain improvements in the rules of the game. But these rules will have to be agreeable to most participants; we cannot impose our rules on the rest of the world. The United States should avoid the self-righteous view which implies the sins are all those of our trading partners. Certainly in terms of measured trade barriers, we are not blameless.

---

[4] For a more complete discussion see Robert Z. Lawrence, Can America Compete? Brookings, 1984, pp. 117-41.

The most straightforward policy guidelines for dealing with such assistance are either (1) to ignore them and to follow a policy of free trade or (2) to match them. Serious problems are associated with both approaches. The free trade approach ignores the strategic considerations inherent in trade policy. The threat of possible retaliation prevents other nations with monopoly power in trade from setting an amount of protection that maximizes their gains from trade. A strong commitment not to protect under any circumstances could leave the United States vulnerable to foreign monopoly power and unable to use reciprocal reductions in protection as a negotiating device. The second approach, to match whatever subsidies foreigners provide their industries, would be impossible to administer and would simply compound the folly. Taking foreign subsidies as given, aid to the same industries as those abroad would lower U.S. national welfare. The United States might produce goods at home that could be more cheaply obtained from abroad. Because foreign governments often grant assistance to declining industries, matching could lead the U.S. to place more resources in the industries that it should avoid.

The general rule toward foreign targeting and subsidies should be to try to deal with these measures only where (i) they clearly damages U.S. welfare and (ii) U.S. government action can make the United States better off. In general, the United States should permit foreign trade even when foreign competitors receive direct government assistance. The mere presence of foreign subsidies need not imply that U.S. welfare will be damaged. This is particularly true of foreign export subsidies on U.S. imports. Some U.S. producers may experience competitive pressures, but U.S. consumers and producers distributing these products and using them as inputs usually have an offsetting gain. U.S. trade laws appear to have made a reasonable compromise in the rules governing counterveiling duties and dumping. Such duties can be levied, but only where imports cause injury. Although they do not exactly require proof that the costs of dislocation to producers exceed the benefits to consumers, these proceedures are a reasonable compromise between consumer and producer interests.

It is much tougher to deal with competition abroad. When foreigners depress U.S. export prices (or sales outside the U.S.) there is no necessary offsetting benefit to U.S. consumers. The United States may have some scope to act strategically so as to persuade others to reduce or eliminate export subsidies by matching them. But this approach should be attempted only if political judgment indicates that it can be effective in leading others to reduce and ultimately to eliminate these practices. Otherwise, taking foreign susbdies as given and blindly matching them will simply make us worse off. The need for strategic behavior in this area suggests that it is best left to the Administration rather than to be undertaken by the Congress. Legislative bodies are inherently unable to provide the coordinated approaches required for successful strategic behavior. While Congress can and should signal the priority it wishes the Adminstration to place in shifting the trading rules, it should not try to enact detailed negotiations on its own. In particular, crude legislative measures, such as several currently before Congress, are more likely to induce foreign protectionist retaliation rather than to open markets abroad.

The United States is also aided by foreign anti-dumping laws, which inhibit "unfair" competition against U.S. exports in third markets. Indeed, I view U.S. antidumping laws, which hurt U.S. consumers, as a contribution to an international order rather than a purely domestic action. The United States must maintain pressures to open up foreign markets both to U.S. exporters and to U.S. direct investors abroad. The approach must have both bilateral and multilateral components. Free trade areas, such as those negotiated with Israel and currently under discussion with Canada, should be pushed forward with other willing partners. In addition, continuous pressures should be maintained in seeking improved access to the Japanese and other markets, by all diplomatic means available (and not those relating simply to trade). Above all, however, improvements in the rules of the trading game must to be sought and obtained. The upcoming GATT round is the appropriate arena for securing these improvements.

Improving the rules of the game and opening up foreign markets to U.S. firms will not, by themselves, lead to a better U.S. performance in international trade. These measures must be accompanied by actions in our domestic macro- and micro-economic policies. An installment plan which draws up a program to bring the large government deficits into balance by the end of the decade by reducing spending and raising revenues is imperative. In addition, programs which facilitate adjustment and aid those dislocated by change should be improved, and positive measures to stimulate innovation and improve productivity should be adopted.

STATEMENT OF MICHAEL AHO, SENIOR FELLOW FOR ECONOMICS, COUNCIL ON FOREIGN RELATIONS, INC., NEW YORK, NY

Mr. AHO. Thank you Mr. Chairman. It is an honor and a pleasure to appear here today to discuss U.S. trade policy, particularly what should be done about unfair trade practices.

We have just heard an eloquent statement by Professor Jackson on how unfairness has become the central trade policy issue. And in that he has focused on subsidies, I would just go on to point out that in the world today there are no purely domestic policies. Obstensibly domestic policies directed at taxes, agriculture, et cetera, can have as much of an impact on international trade flows as tariffs or quotas; the problem is that we lack a multilateral definition of what is fair. Unfairness is in the eye of the beholder.

We accuse Japan of industrial targeting in high technology industries, but what about the Strategic Defense Initiative, or even our agricultural extension service, for that matter?

My preference in attacking unfair trade practices would be to look at them in the context of a new round of multilateral trade negotiations, but not a usual round which stretches out, in which Congress delegates at the beginning of the round the authority to negotiate and then becomes in at the end to implement that round.

I would look at a round in which Congress and the private sector play a more active role. One of the primary objectives in that round that I will stress, however, is to improve international discipline.

Ambassador Yeutter was correct last week when he said that the GATT system is crumbling. The Democratic task force in its report talked about GATT being in disrepair. I would agree with both of those, but I would also underline that we need a multilateral system.

Consider a few questions: How will the United States be able to generate current account surpluses of up to $100 billion to service its trillion-dollar foreign debt in the 1990's?

How can the heavily indebted countries generate sufficient export earnings to service their debts in a fragmented trading system? Both are unlikely, should that system fragment.

However, I do not underestimate the complexity of attacking these unfair trade practices in a new round. Indeed, in a new book, I have argued with my coauthor Jonathan Erinson, that the coming negotiations will be more difficult, more complicated, and last longer than any that preceded them.

A list of 10 significant challenges which will give negotiators a tough time in these coming negotiations is attached to my testimony. These negotiations could last a decade.

Well, how can we structure those negotiations in a way that on the one hand maximizes U.S. negotiating pressure or negotiating leverage, if you will, and come out with something at the end of the day which in fact improves this multilateral system?

Well, one of the things we are going to have to do is to make certain that we are not just focusing on yesterday's problems. A negotiation that lasts that long will require that negotiators incorporate what they learn as they proceed in the negotiations. But more importantly, I would argue that the United States is going to have to maximize its leverage through greater congressional involvement and greater private sector improvements.

And there what I might suggest—and I know several bills are now appearing that would extend U.S. negotiating authority beyond January 3, 1988—I would suggest that Congress establish intermediate deadlines in the delegation of authority—say at 3 years, 6 years, and then at the end of the period, say for 10 years. I say 10 years because, if this round is to be ambitious and it is going to attack unfairness and institutional reform, and agriculture, and all of the other problems that are plaguing the trading system, we are going to need at least 10 years. But if we had intermediate deadlines, then the United States would have more of an opportunity to push the process along.

Why only use congressional leverage—and Congress is the only threat the United States has which people believe overseas—why only use that leverage before negotiations begin and at their conclusion?

Another advantage to this approach is to compel the administration to take action on trade policy issues. This country does not focus upon trade or competitiveness issues until it is focused to by Congress, as recent events have demonstrated. As deadlines approach, this would ensure that trade receives the higher level political attention, and it will force decisions.

That is not to say that there is no role for national action as we go into these rounds. I suggest in my testimony that maybe what we ought to do is develop wish lists of what we are looking for from the rest of the world. The recently released National Trade Estimates is a step in the right direction; what we ought to be doing is tabling those wish lists, and other countries will do the same, and then discussions can be done in earnest. Only in that context can an international consensus emerge on what is fair and what is not fair.

But even then—and this brings me back to a stronger argument at the end of the testimony for GATT reform—we are going to need changes in order to keep the system evolutionary, to keep up with the changes in the world economy today.

Senator Bradley, before he left, mentioned that GATT wisemen's report. There were several suggestions in there; there are some more in my testimony for reform. I noted them yesterday also in the bill that was introduced. It was in the Democratic task force. I hear a lot of people talking about reform, and I think that institutional reform will be the key ingredient.

Let me finish, though, quickly, in saying that the only time the United States comes close to articulating a coherent trade policy is in the context of a new round of negotiations. And I would call upon Congress, in drawing up that negotiating authority, to structure them in a way that the round becomes a way for resolving issues, not postponing them.

With that, I'll stop.

(Mr. Aho's written testimony follows:]

TESTIMONY ON
U.S. TRADE POLICY AND UNFAIR TRADE PRACTICES

BY

C. MICHAEL AHO
SENIOR FELLOW - ECONOMICS AND
DIRECTOR OF THE INTERNATIONAL TRADE PROJECT
COUNCIL ON FOREIGN RELATIONS, INC.

BEFORE THE COMMITTEE ON FINANCE
UNITED STATES SENATE

NOVEMBER 20, 1985

Mr. Chairman and members of the Committee, it is an honor and a pleasure to appear here before you today to discuss U.S. trade policy, particularly what should be done about unfair trade practices by other countries.

Unfairness has become the central trade policy issue. The world has become so interdependent and world economic integration has proceeded so far that the distinction between domestic and foreign economic policies is obsolete. There are no more purely domestic economic policies. Internal conditions in individual economies are quickly transmitted across national borders through trade, technology and financial flows. Ostensibly "domestic policies" directed at taxes, agriculture, regional development, or investment have as much impact on international trade flows as tariffs or quotas.

Attempts to deal with the trade effects of "domestic policies" are viewed as infringements of sovereignty and quickly become politicized. Questions of unfairness are raised. If the microeconomic "domestic policies" of one country injure firms and workers in another country, the second country promptly claims unfairness, demands redress, retaliates, and resists further reduction in its own trade barriers. To proceed in this fashion undermines the trading system.

The problem is that the trading system lacks a multilateral agreement on what is fair and what is not. In the absence of multilateral agreement on which policies are acceptable, countries are unilaterally adopting their own definition of unfairness and these definitions are inconsistent internationally. The United States accuses Japan of industrial targeting and of using restrictionist policies to encourage the development of new industries, but what about U.S. defense procurement (e.g. Strategic Defense Initiative, NASA etc.) and our agriculture extension service? Unfairness is in the eye of the beholder.

Subsidies and government procurement go to the heart of the fairness question. But rules on subsidies and other nontariff barriers under the General Agreement on Tariffs and Trade (GATT) are not as fully accepted as the rules on tariffs. A major challenge facing the trading system is to define what a subsidy is and when it is legitimate to use them. Industrial policy, natural resource policy, tax policy and many other kinds of subsidy can bestow unfair trade advantages. Explicit subsidies can be countervailed against, but government procurement policies and subsidies for research and development (R&D) at the outset of industrial development can bestow advantages which last for years. I realize that Congress is contemplating reform of the unfair trade practices statutes to broaden the definition of unfairness but if the United States does that, other countries are sure to follow. If that happens, U.S. firms which benefit from defense R&D and procurement will likely face higher barriers overseas after other countries revise their trade laws.

My preference is to address these practices in the context of a new round of multilateral trade negotiations. Trade negotiations have usefully served in the past to maintain the trading system and to liberalize trade. But they have been less successful in establishing rules and disciplines to cover nontariff barriers and domestic practices which distort trade. Furthermore, new issues like services (including telecommunications) and intellectual property protection have emerged which are not covered by existing rules. Unlike in past negotiations, the policy dilemma in new negotiations is not one of free trade vs protectionism. It is a question of rules and discipline, of who obeys and who does not and of what is fair and what is not. Unless international discipline improves, it will become impossible to convince citizens and firms that they should obey the rules when they believe that no on else is playing by them. If present trends continue the trading system will end up fragmented, and everyone will lose.

Consider a few questions. How will the United States be able to generate current account surpluses of up to $100 billion to service its trillion dollar foreign debt in the 1990s? Without an open multilateral trading system, that will be next to impossible. Could the heavily indebted countries generate sufficient export earnings to service their debts in a fragmented trading system? Unlikely. Finally, could the dynamism demonstrated by South Korea, Hong Kong, Taiwan, and Singapore be replicated in a fragmented trading system? I doubt it. These countries are now among the top twenty exporters and importers. That dynamism would not have been possible without a multilateral trading system. Before taking steps which could fragment and destroy the trading system, we should redouble our efforts to strike a multilateral bargain.

I would not and I do not underestimate the complexity of attacking the problems in a new round. Indeed, Jonathan Aronson and I have argued in our new book (Trade Talks: America Better Listen!) that the coming negotiations will be more difficult, more complicated, and last longer than any that proceeded them. A list of ten significant developments that will challenge the ingenuity and determination of the negotiators is attached to my testimony.

In that book we conclude that the world trading system and the world economy are likely to diverge from the rules of the trading system faster in the future than in the past. Unless more flexible ways of making certain that the rules continue to evolve in step with the world economy are found, the coming trade negotiations will solve little and may even hamper the ongoing worldwide economic adjustment process. What is needed is a way for negotiators to incorporate what they learn as they proceed in their negotiations. This is essential for negotiations which could last almost a decade. Greater reliance will have to be put on establishing ongoing processes and procedures which can examine new developments as they arise in order to assess their importance and policy implications. What is also needed is a firm U.S. position on what it wants to get out of the negotiations and a strategy for obtaining those objectives. How should the U.S. maximize its leverage?

Congress again will play a critical role in shaping the negotiations and ultimately in implementing any agreement. But these negotiations require a different approach than the one taken in previous negotiations. If they are going to be ambitious and are going to tackle unfairness, services, agriculture, institutional reform, and the host of other problems afflicting the world trading system, they will require years of analysis, discussion, and negotiation. But we cannot wait that long to make progress on many of these issues. I would propose that Congress establish intermediate deadlines in its delegation of authority. Congress could mandate that preliminary packages be put together after, say after 3 and 6 years, with final agreement set at 10 years (all with fast-track consideration). Any agreements reached at the intermediate deadlines could contain contingency clauses which would abrogate them if future progress was not forthcoming. This would maximize U.S. leverage. After all, the biggest threat the United States has and the only thing that motivates other countries to action is the fear that Congress might pass something protectionist. Why only use that leverage before negotiations begin and again at the conclusion of negotiations?

Another advantage of this approach is to compel the Administration to take action on trade policy issues. Other countries make a point of using top-level political officials to intervene in trade disputes. This country does not focus upon trade or competitiveness issues unless it is forced to by Congress. As deadlines approach, this will ensure that trade receives higher-level political attention and it will force decisions.

Some may object because such an approach gives Congress a more important role in the conduct of trade policy but that is happening anyway. I feel this would be preferable to establishing mandatory procedures that require retaliation or impose restrictions. I would argue for leaving the Executive Branch with the flexibility to negotiate. Mandatory procedures actually reduce U.S. leverage in such negotiations. A tit-for-tat approach would represent a radical departure from past U.S. policy and if other countries emulate it, which seems likely, the trading system will be further undermined, not improved.

That is not to say there is no role for national action under the our trade laws during the negotiations. Specific trade policy issues will arise and invoking such procedures from time to time will be necessary in order to move the multilateral process forward. Without continuing high-level political involvement and active support from the private sector, sustaining these new negotiations over the course of a decade will be next to impossible.

To handle specific trade problems and to mobilize the private sector behind the negotiations, all countries should develop "wish lists" of foreign barriers or practices that it wants removed. The recently released National Trade Estimates is a step in the right direction. USTR, in consultation with the private sector, should be developing an inventory of foreign practices that it wants to eliminate. These should form the basis for the negotiations. All countries could table such "wish lists". As new issues arise, they could be added to the list. Only after an examination and debate on the merits and demerits of the various national practices in a multilateral forum can some kind of international consensus emerge on what policies are acceptable and which are not. But in some areas it will be impossible to write new substantive rules. (The U.S., for example, will not substantially change defense procurement policies.) And even with a more explicit multilateral agreement, subsidies or other policies used for domestic purposes will always create empirical questions about the extent to which they affect trade and cause injury to foreign economies. Nonetheless, procedural rules could be adopted to help mediate disputes that arise. A complaints procedure, short of formal dispute settlement, is needed for mediating and for resolving disagreements over national practices.

These changes will help but by themselves they will be insufficient to cope with the disputes caused by disagreements over unfairness. Other institutional changes will be needed to strengthen trade discipline and to improve trade policy formulation both internally and internationally.

At the international level, several reforms are needed to update and enhance the GATT; the adjudication of disputes and enforcement of rules needs strengthening; GATT should become more of a forum for mediation and conciliation of trade policy issues that are not explicitly covered by existing rules; GATT should be reformulated so that the system can respond to problems as they emerge. Ultimately, GATT needs to become more respected so that it can be leaned upon by national policy-makers. Specifically:

** Governments need to be held more accountable for their trade policies. They should be required regularly to explain and defend their overall trade policies. The GATT Wisemen's'group which Senator Bradley sat on (Trade Policies for a Better Future: Proposals for Action) recommended that each year a panel representing three to five governments should be established to review a GATT Secretariat report on the trade policies of each of the major industrial countries (less frequently for smaller countries), subject its representatives to questioning, and make recommendations. This surveillance procedure is similar to the OECD economic reviews and could also serve to review existing restrictions and safeguard actions.

** A strong independent international component is needed to operate in the general interest and enforce the rules and norms. No one is tending the trading system at the present time. The GATT Secretariat should be empowered to initiate studies of national trade policies; to collect, maintain, and publish comprehensive information on trade policy measures and actions. It should also be given the authority to call meetings and set agendas.

** To promote confidence in the system, dispute-settlement panels should be set up and should complete their work more speedily and should always clearly indicate the rationale for their findings. One of the delays in dispute settlement cases occurs when a panel is being put together. The GATT Wisemen's report called for establishment of a permanent roster of non-governmental experts familiar with GATT matters who could be called on to serve on panels. A cadre of expert panelists would help to minimize the political influence on dispute panels which is inherent in the current process. Such a panel of experts is similar to the administrative law judges in U.S. labor relations cases and the board of experts which serves the U.S. Nuclear Regulatory Commission. Dispute-settlement procedures would also be improved if the Director-General of GATT were authorized to initiate mediation and conciliation at an early stage.

** GATT's role as a forum for continuous negotiation should be developed. For GATT to be effective, political commitment and more frequent eye-to-eye contact to increase peer pressure are required. To keep abreast of recent developments and to minimize potential conflicts trade ministers should meet more frequently as their financial counterparts do at the IMF and World Bank annual meetings or as the leading monetary authorities do monthly at Basel under the auspices of the Bank for International Settlements. A standing ministerial-level body should be established to serve as an executive committee to move issues along or to address them before they become full-blown.

Domestic reforms are also necessary. Disraeli once remarked that in international trade there are no principles, only interests. True enough, but the problem is that all interests are not heard from. Trade policy is a domestic policy decision because changes in trade policy have distributional consequences. The problem is that the stakeholders in open trade are relatively silent. They need to be mobilized. Furthermore, in most discussions of trade policy the right questions are seldom asked. If legitimate issues of worker adjustment or national security are involved, are import restrictions the most efficient policy available?

If Congress is going to play a more active role in trade policy, it needs better information on the costs and consequences of various policy options. What is needed is an impact statement similar to the environmental impact statements now required in many public works projects. Currently, on an ad hoc basis, the FTC and Brookings have done estimates of the costs and benefits of protection in various industries. The CBO did such an analysis for steel last year. But nowhere is there a requirement to conduct such an analysis on a regular basis.

In sum, institutional reform will be the critical ingredient for ensuring that the trading system evolves in response to emerging problems. Internal and international reforms could be mutually reinforcing. Stronger international discipline could reduce the number of unilateral actions. Internal decisions resulting in fewer unilateral actions could enhance the credibility of the system and its discipline. Above all else, any agreements reached in these negotiations will have to contain mechanisms for updating rules and norms on a multilateral basis as circumstances change. Otherwise countries will fall back on unilateral interpretations or ignore the agreements altogether.

* * *

A complaint frequently heard today is that the United States does not have a coherent trade policy. But the only time the United States comes close to articulating a coherent trade policy is in the context of a major multilateral round of negotiations. I would urge that we get on with it. In order to ensure that trade policy continues to receive high-level political attention and to mobilize private sector support, Congress in drafting the negotiating authority should structure the negotiations so that the round becomes a way for resolving issues, not postponing them.

APPENDIX

(Adapted from Trade Talks: America Better Listen!
by C. Michael Aho and Jonathan David Aronson
Council on Foreign Relations, 1985)

Ten Policy Challenges:
Why New Trade Negotiations Will be Different and More Difficult

1.) Economic interdependence has proceeded so far that the distinction between domestic and international microeconomic policies has been rendered obsolete. Unfairness has emerged as a central trade policy issue because there is no international agreement over which policies are acceptable and which are not. What's more, many international transactions today do not cross borders in the traditional way, but instead are carried over telephone lines and beamed by satellites. Regulation is more difficult to conduct. In many areas, national regulatory structures will be the focus of the negotiations.

2.) U.S. preeminence has declined and it can no longer lead negotiations alone. Furthermore, international economic integration has provoked a strong domestic reaction, as domestic political forces have mobilized to resist internationally induced economic change as never before. Even if the United States could still dictate economic terms to the rest of the world, it is no longer willing to do so. Joint leadership is necessary but it is less stable and more prone to delay than a system dominated by a single country.

3.) A related development which complicates decisionmaking is the increased pluralism in the trading system. More countries will play a critical role in the negotiations. Bargaining diplomacy has replaced power diplomacy as the mode of operation. But international discipline is a public good. In a bargaining context, it pays for countries to understate the benefits they derive from the system.

4.) The world has entered an era of slower economic growth and higher unemployment. Although technological advance is reshaping national economies and is usually the primary cause of economic growth, in this case it is not leading to much net job creation. With significant worker displacement, occurring, workers and their elected representatives are more reluctant to support policy changes, like trade liberalization, which could result in more displacements. The conflict between the need for economic adjustment in order to increase growth and the political pressure to erect obstacles to adjustment will continue and probably intensify in the future.

5.) The easy things have all been done. Except for politically sensitive industries like textiles and apparel, tariffs have been reduced significantly during the previous seven negotiations. Those negotiations were relatively straightforward because tariffs are transparent and easy for policy-makers to follow and understand. By contrast, the nontariff barriers which now are the biggest obstacles to open trade are not transparent, not easy to quantify or as susceptible to reciprocal negotiations.

6.) Excess capacity in basic industries is a growing problem. In sector after sector the world can grow, build and produce more than it can sell, deliver and consume. The challenge is to allocate production and to assure distribution. Markets could do both, if only governments would let them. Instead, government interventions are widespread and the world economy is drifting into regimes of managed trade in several major sectors. Once begun, it is hard to get out of such regimes because vested interests form with a stake in their continuation.

7.) Many countries are using industrial policies to create competitive advantage, particularly in the technologically advanced sectors. Governments are intervening in the market to support R&D and promote technological innovation and to bestow advantages on their firms which can last for years. But there is no multilateral agreement on what constitutes legitimate support for the development of an industry. Are technological policies negotiable?

8.) Sectoral distinctions are breaking down. The merging of telecommunications and computing technologies is creating a world information economy. Financial supermarkets are emerging in place of separate banking, finance, insurance and brokerage activities. Trade negotiators lack the competence or authority to negotiate in many of these areas.

9.) The shape of global competition is changing as firms from different countries are forging complex alliances in different sectors. Joint venture strategies and cooperative alliances have divided the world market up in different sectors among coalitions of competing internationally based alliances. Interests cut across national boundaries in complicated ways and this raises questions about the continued support of multinational firms in efforts to liberalize trade. The discontinuity between the way multinational firms view the world and the way governments are structured to deal with the world is growing.

10.) A final complicating factor is time. The interval between the development of an idea and its commercial application has shortened. Product obsolescence is reached faster. Product life cycles have diminished. In a world in which technology can change the conditions of competition almost overnight, improved procedures for resolving issues on a timely basis are essential.

The **Chairman**. Mr. Lawrence, you have heard me ask the question, yesterday and today, about the argument of the low wage and the differential and the industries that say they cannot compete. They are not looking for a temporary adjustment period; they are looking for permanent protection, and some of them are frank enough to admit it. Or others will phrase it that the wage differential is unfair trade or ought to be unilaterally defined as unfair trade, and therefore we'll apply whatever unfair trade sanctions we want to it.

What do we do with those industries that cannot compete? I mean, we will have trade adjustment, or we will try to, and you try to gently help them; but should we permanently protect them?

Mr. **Lawrence**. Well, in short, I think that we cannot provide permanent protection. We have to understand what determines wage levels in two countries. Why are wages, broadly speaking, lower in one country than another?

Now, much of our discussion—because we are worried about international trade--focuses on competition that occurs between our firms and firms in the rest of the world. But there is a second kind of competition that is occurring within the United States, within the U.S. labor market, for firms that are trying to attract labor to work for them. And the reason that our wages, broadly speaking, are high is that our productivity levels in this Nation are high. Basically, to keep workers in, for example, the textile industry, it takes a $5 or $6 wage, because if a firm doesn't pay that wage, the textile workers, will go and work somewhere else. They may go and work in services, or they may go and work in some other firm; but it is important to understand that our basic wage level reflects our higher productivity.

Now, broadly speaking, nothing will guarantee that if we have high wages in this country, every industry will be able to afford to pay those wages. And indeed, what we find is that some industries don't complain about the higher wages they must pay while others do.

The fact that some industries discover that they can no longer pay the going wage in the United States and still make a profit is a very important market signal. In general, it suggests that, the activities of that industry, ought not to be performed over the long run in the United States.

I would submit that the ability to obtain goods abroad cheaply is a major way in which we ourselves can raise our living standards.

We heard a lot of discussion yesterday about how industries ought to keep wages high just by protection or by any other means required to raise living standards. I would argue the very opposite: A country gains advantages through its ability to trade precisely because it can obtain certain products more cheaply from the rest of the world and can therefore allocate its labor to those firms who can pay the going wage.

So generally, I think that we must adjust to those trends determined by the international trading system. I do see two exceptions, though: The first occurs in the area of national defense. However, I would not take the next step and advocate the use of trade protection to meet our national defense needs.

Let us take the automobile industry as an example. Now, I think we would all agree that that Chrysler plant that manufactured tanks was crucial to our national defense. But it would seem to me that it would not be necessary to protect an entire industry. Because of our concern about national defense what we ought to do is to say to the Defense Department:

> You are the experts in national defense. We as a society will give you a budget. Now, you trade it off. If you think we need another bomber system, spend your dollars on that. If you think we need a steel plant to be kept at idle capacity, spend your dollars on that.

So, I would not take that second step, which suggests that trade protection is the correct way to meet our national defense needs. I agree that a free market will not give us the defense base we need; but I think we as a society should determine how much we want to spend on defense, and then we will let the Defense Department allocate those dollars.

The CHAIRMAN. You know, interestingly, that is almost what we do with our Buy-American provision on military ships. Commercial ships? We can build them anyplace, and most of them are built overseas. We just say that military ships have to be built here, and the Defense Department gets money, and then pay shipyards to build the ships. That is what keeps many of these shipyards going, and that is a form of the Defense Department using their money, in essence, to keep what would otherwise be an idle or closed shipyard in business.

Mr. LAWRENCE. True, but I would prefer to say to the Defense Department:

> Here is your money. You decide how you are going to spend it. Now, if you think we need to build ships, we should build them as cheaply as we can. On the other hand, if you think we need shipbuilding capacity in this country, then you should try to trade off the cost of keeping that shipbuilding capacity in this country against other kinds of money that you spend.

The CHAIRMAN. Well, in essence, that is what they do. I shouldn't say they need ships, because we could build the ships overseas; what we need is a shipbuilding capacity. If the Defense Department says we need a shipbuilding and ship repair capacity then the only way to have it is to build some ships here, or we won't have any ship repair capacity.

Mr. LAWRENCE. Respectfully, I would like not to have a legislative provision which makes them build the ships here. I would rather simply say to them, "Your budget must include taking care of our national security." Because that way, we as a society will get an efficient outcome.

Every industry that seeks trade protection can legitimately argue that elements in that industry are required for national defense. But I think an efficient defense-rated policy would allow the Defense Department to be the arbiters of what we really need for our national defense.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. Following up on that same point, it just seems to me if we were to pursue that route—this is a new idea—that we would have to increase the Defense Department's budget.

That leads me to ask the question as to the degree to which you think that our competitiveness or our trade deficit is attributable to the free ride we are giving other countries in providing them our national security umbrella. One percent of Japan's GNP is on defense, and in the United States it is about 7 percent. In Japan and the European countries, they spend a much lower percent of their GNP on defense. Yet, we are providing them basically the security. So my question is: To what degree is the United States footing the defense bill in the free world a part of the problem here?

Arguably, those dollars could go to subsidize lower interest rates, or to all kinds of ways. And better infrastructure? That is a cost of doing business in this country. There are all kinds of areas where those dollars could otherwise be spent. We could tell Japan and other countries, "Look, you have got to pay your way from now on."

Mr. LAWRENCE. Well, Senator, I am no defense expert, but I do believe that a major component clearly of the source of our budget deficit today, which ultimately I have linked in my testimony to our competitive problems, relates to our increased defense expenditures.

I also find it quite peculiar that we have accelerated our defense expenditures without a concommitant commitment on the part of our allies to at least do the same. And in particular, if you stand back and think that when we began our post-war era, our incomes were 50 percent higher than those of our trading partners in Europe, and about 80 or 90 percent higher than the Japanese. At that time there was some logic to saying that we could shoulder more of the umbrella of defense. But if you stand back and say that living standards today are converging around the world, that our real incomes are not much higher than theirs, then you start to wonder why it is that on a per-capita basis Americans should be providing this unbrella.

Now, of course we have to recognize that it will involve less flexibility on our part in exercising our national sovereignty in the defense area, but nonetheless I do personally believe that, given their higher incomes today, they ought to be providing more of that defense umbrella.

Senator BAUCUS. Do the rest of the panelists agree, or disagree?

Professor HUFBAUER. Senator, I would say that if we did persuade, say Japan to shoulder a larger share of defense spending, either done in Japan or contributed to the Pentagon, that would in itself make only a long-run difference in the trade deficit and would not answer most of our unfair trade concerns today.

Senator BAUCUS. I understand that, but is that a component?

Professor HUFBAUER. I would say it is a long-run component. That is a component that would show up in 1995.

Senator BAUCUS. It is not too far away.

Professor HUFBAUER. You take a long-run perspective.

Senator BAUCUS. Changing gears slightly, basically as I understand it the two of you, Dr. Lawrence and Professor Hufbauer, you are saying that most of our problems are problems we should take care of ourselves—get our Federal budget deficit under control so our goods are not so highly priced as compared to other countries, have better adjustment programs, and so forth, youthful autrop art, you mention a little bit about the Latin debt problem, and other countries, and that is important, too.

Yet, you, Dr. Aho, concentrate pretty much on if not a new GATT round then some new approach to get the countries agreeing together, and so forth. I infer from what you say that is part of the problem, maybe a longer term, not so much short term.

Do the two of you, Professor Hufbauer and Mr. Lawrence, tend to disagree with Dr. Aho? Or do you, Dr. Aho, tend to disagree? You have different approaches to this, and I am trying to figure out why.

Professor HUFBAUER. Senator, because of the confines of time I used up my 15 minutes on the macroeconomic side, but much of my written testimony deals with unfair trade policy issues. I think they are very serious.

Senator BAUCUS. By definition, that is less than 15 percent of the problem, according to you.

Professor HUFBAUER. It is not a big part of the trade deficit problem, but it is a very big part of the trade policy problem because unfair trade is a major grievance to U.S firms.

The United States spends a lot of legal effort on the import side of unfair trade. Where our real weakness lies, and where I devote a good deal of my written testimony, is on the export side of unfair trade policy. That is where we need to concentrate our attention.

Dr. AHO. And I don't disagree with their economic analysis. I think I might go for 75 percent rather than 90 versus 60, but the dollar is the big problem. We have to attack those things on a parallel track.

But when we see on the unfair track side is, it is undermining the discipline and the respect for the system. It gets harder to tell our citizens and firms that they should obey the rules when no one else, in their mind, is obeying the rules.

Senator BAUCUS. Thank you.

Mr. LAWRENCE. In my view, if you are trying to explain this trade deficit, I don't think that either unfair trade practices have a lot to do with it currently or that making the world more fair to American products would have a great impact in improving the trade deficit, because I see trade deficits as fundamentally being driven by national spending patterns. A trade deficit tells you a country is borrowing. That, in turn, must mean either its government is borrowing or its private sector are borrowing. And when you change particular goods that are coming in and out of a country, you don't necessarily influence those ultimate borrowing decisions which drive the trade position.

So, I don't see that the issue of fair or unfair trade is germane to the question of the current size of our trade deficit.

I, too, in my testimony, discuss how we should respond to unfair trade practices and concur that the emphasis of policy now has to be on that unfair trade practices in third markets. But I do think that, ultimately, if we are to have a growing international trading system, making sure that there are rules of the game that are crucial, and we have to improve the current rules of the game.

So I see it more as a longrun approach. The tensions have been heightened now because of the difficulties our firms are having in competing. But really, even if the dollar were to be undervalued, not overvalued, we would still have to take measures to make sure that that playing field is level.

Senator BAUCUS. Thank you.

The CHAIRMAN. Senator Long.

Senator LONG. The situation we are involved in currently is an area where all roads lead to debt. But I suspect if you didn't have this overvalued dollar, you would find that there are other reasons why we have this huge deficit.

Now, looking at Japan, I suspect you find that with or without the overvalued dollar the Japanese Government and its business community, working in concert, have made a conscious decision not to have the kind of debt we have here; I think they would eat what they are eating rather than eat more beef, for example, and that the people would be just as well off getting protein out of soy as out of beef, and that on the whole their people are just as healthy with the diet they are eating than they would be with our diet. So, they would just as soon keep it that way.

It seems to me that that it may have been a conscious decision, to keep the people of Japan living in very limited housing, only a fraction of the amount of housing that we have for the average family here. And apparently their plans dictate that things are going to stay that way for a long time to come; likewise, that they are not going to have many more automobiles over there, even though they can produce a great deal of them; they are not going to have the land for parks and playgrounds for their children to play baseball, or whatever: and they are not going to have the golf courses that they ought to have for people who would like to play that, or even tennis courts. You know, there is not the land for public use there that we have in this country.

It is part of a conscious decision to save and invest rather than to spend and to go into debt, and that creates problems for others, solving their problems at our expense, provided that they are right in the solution they are working toward.

I would just like to know your reaction to it.

Professor HUFBAUER. Senator, I think that is a fair and good question. In testimony I gave to this committee in June of this year, I took a rather skeptical view on what I call the fraternal twin thesis, namely the supposed close connection between the U.S. budget deficit and the U.S. trade deficit. I looked at the statistics, and that thesis only holds up in 3 out of the last 10 years, which means it doesn't hold up in out of the last 10 years.

So, I don't think you can say with confidence that, if we reduce the budget deficit, we will shortly and to the same extent reduce our trade deficit. I don't want to be associated with that thesis.

I do say, however, that the exchange value of the dollar is decisively important. For reasons that were referred to earlier, it is not automatically certain that, if the United States reduces the budget deficit, the dollar will come down in the foreign exchange markets. That is my first point.

My second point concerns your comment that a great many Japanese policies are biased against imports. I attempted to estimate what might happen to bilateral United States-Japan trade if Japan completely liberalized—not only reform at the official level but also reform of the quasi-cartel system which permeates much of Japanese industry. My estimate, which is admittedly rough, and is higher than estimates made by some of my colleagues, is that about $10 billion of additional United States exports could be generated after a few years, if Japan is completely liberalized.

Now, if Japan further changed its policies to deemphasize savings and to encourage, for example, more housing construction, that would no doubt do a great deal more for the trade balance.

These are not trivial policy changes. I recognize how hard it is to persuade another country to change its trade policies much less its basic savings and investment policies.

Mr. LAWRENCE. Senator, I agree with the basic perspective which you have provided, which, I think, is to point to the role of any country's, decisions to consume instead of saving and decisions to invest as being the key determinants of its trade surplus or deficit position.

And I do see the large and growing Japanese trade surplus as a reflection of an underlying high savings rate in Japan, matched now by a somewhat declining domestic investment rate. So they are not using that money at home; their Government has also now moved to tighten its budget deficit, so the Government isn't absorbing those savings, and those savings are, therefore, available for use in the rest of the world, which is driving them into running these significant trade surpluses.

I think that takes us to the point that if we perceive these surpluses as a major problem in the trading system, if they are occurring too rapidly for us to absorb them, and, indeed, at times, I think, they are, then we must, instead of talking to them, try to open their markets. But if it is the trade surplus or deficit that we are trying to affect ultimately, we must look at the policies which influence their spending and savings decisions, and that involves macroeconomic coordination, and not necessarily trade policy.

So, I do think, that ultimately the reduction of our trade deficit will require changes in our spending patterns, and the reduction in their trade surplus will require changes in their spending patterns. In a sense, the frictions which the trading systems are being placed under are simply a reflection of some more fundamental forces at work, and if as policymakers we want to try to improve the situation, we have got back to those root causes.

Dr. AHO. Senator, just like two households where one is living beyond its means and spending more than it is earning and the other one is saving a good portion of what it earns, what is the longrun implication of that pattern? We will end up by spending more than we will earn, and we are going to end up having to service that debt down the road, and those imbalances are going to remain out there unless there are these corrections in spending and savings patterns.

The CHAIRMAN. Senator Bentsen.

Senator BENTSEN. Thank you very much, Mr. Chairman. As I listen to this, I can't help but think how we are faced every day witht the problem of translating economic theory into reality. Now we do it in a Democratic process. And as I listen to some of these things, I can't help but question the long-term results—I don't know how long that long is, and I don't know how many people drown along the way trying to get there.

But, I think, it is the height of arrogance for us to say to the Japanese, "You have got to save less, you have got to spend more on housing, you have got to change your cultural habits." That is within their province.

I think free trade presupposes some reasonable balance in trade, or else you have the impoverishing of one nation and the enriching of the other. There must be a way to allow countries the time to make the adjustments that you fellows are talking about; it is not going to happen overnight, and I am not willing to accept what, I think, has to be a very substantial, severe economic dislocation in the short run. I want to buy the time to try to do it in a democratic way, where we can adjust to it.

Now, Professor Jackson was talking earlier about these different things you are talking about resulting in large trade imbalances, and as I understood it, he was suggesting that perhaps you have to find something in the way of tariffs to buy the time to bring that about.

I noticed, Dr. Hufbauer, on page 8 of your testimony, you suggest that perhaps one of the best ways to break down unfair foreign trade barriers to U.S. exports is an across-the-board duty on imports of the recalcitrant country. I listened to you say $10 billion, I hear others say $14 billion—I don't know what the number is—the amount of products they would accept of ours if they didn't have these barriers.

Tell me why you think an across-the-board duty like that is better than one done on one product.

Professor HUFBAUER. Excuse me, I didn't hear the last of that.

Senator BENTSEN. Why do you think it is better, if you had to try additional tariffs, to say we will put it across the board rather than picking out individual items? I very much agree with that, but I just want to hear you tell me.

Professor HUFBAUER. Senator, your question gets to the strategy of trying to deal with closed markets that we find abroad. Virtually all of the prepared remedies come back to one of two things: denying foreign firms access to our market, which is obviously within our prerogative to do, or subsidizing our exports, which is also our prerogative to do.

I come to across-the-board approach by a process of elimination. Historically, we have always been short on providing funds for anything that resembles the subsidization of U.S. exports, through the Ex-Imbank or other means. We have a 40-year record of not providing very many resources in this direction. I don't see that record changing, especially in light of current budget stringency.

That brings us back to denying market access as the principal tool for opening markets abroad.

I am very concerned about methods of denying market access that would entice industry groups to pursue the following kinds of strategems:

An industry association might say: "Our real goal is to open the Korean market for construction equipment." That is what they would say publicly, but the industry group might as well design a strategem which would say, "If the Koreans don't open their market for U.S. construction equipment, what we will do is deny them access to the U.S. market for construction equipment."

Now, if the remedy involves denial of a very targeted market, I can imagine an industry in this country, really thinking that its goal was to close the U.S. market, saying to itself in private sessions: "Sure, it would be nice to get the foreign market open, but we don't see that as a realisitic goal, and our real goal is to close the U.S. market from foreign competition." I don't want to create that kind of incentive.

Senator **BENTSEN**. I don't, either, and I agree with that. And I see my time has expired.

Mr. Chairman, I am always amazed at how short my 5 minutes are. [Laughter.]

Senator **BENTSEN**. And how long everyone else's are. [Laughter.]

Senator **BENTSEN**. Thank you.

The **CHAIRMAN**. Gentlemen, we have a vote. I am going to suggest we take about a 10-minute recess. I will be back here at about 12:10, and we will go on.

Do you want to ask these witnesses any more questions?

Senator **BAUCUS**. I will yield to the Senator from Texas.

The **CHAIRMAN**. We have a few minutes. I think we ought to try to finish up with these witnesses if we can, and at least I will be back in about 10 minutes.

Senator **BAUCUS**. I have one very brief question.

You talk about spending patterns, particularly Dr. Aho and Professor Lawrence. Do you break that down into private and public spending patterns between, say, the United States and Japan?

Mr. **LAWRENCE**. Well, in the case of the United States——

Senator **BAUCUS**. And the relative importance of each, if you will.

Mr. **LAWRENCE**. I understand.

In my view, if we are trying to worry about what kind of impact our national spending patterns have on our trade deficit, if you go back over the last two decades, what you find out is that prior to 1980 we had a tendency to be roughly in balance. In fact, in each of our three sectors—the Government sector may have a deficit of about 0.5 or 1 point of GNP; the private sector as a whole would tend to have savings and investment that were quite closely matched, both running, in gross terms, about 16 or 17 percent of GNP, and that includes both business and personal; and then, the trade sector, therefore, which is the third component, would be roughly in balance.

So you look at that, and you say, "OK, we as a Nation didn't have a very high savings rate, but our investment rate matched our savings rate, and therefore we didn't have to borrow a lot from the rest of the world, given our government budget situation."

Now, what changed after 1980? In fact, our private sector didn't change very much. The savings rates moved cyclically together, so it was higher in 1984 than it was in 1980; the investment rate picked up a little bit; but basically our private sector could have financed all of the investment that had increased, by which it increased investment spending, without borrowing anything from abroad. So the private sector's net borrowing didn't change.

We have the government sector now with a 3-percentage point rise, and we found that the trade sector started to run deficits of that magnitude.

So I think in our case, you know, the dominant change came in the government sector, and that is why I don't think it is really good evidence. Of course there won't be a tack link every year in small changes between the government deficit and the trade deficit; but as a long-run proposition, it almost an identity—it has to happen. If the private sector doesn't change it spending patterns, the government sector will show up as a trade deficit.

Now, if your look at the Japanese, there I can't give you the numbers in great detail; but, in Japan after 1973, after the OPEC oil shock, the Japanese economy slowed down. Until then, it was growing at a tremendously rapid pace, maybe 8 to 9 percent a year. Since that time it has grown on a plateau of probably 4.5 to 5 percent. And in response to that, their investment rates declined quite considerably. Their savings rates didn't come down commensurately.

On the other hand, the initial response of the government sector in Japan was to run a bigger deficit. So in a sense, the government sector started to absorb that excess of savings that the Japanese were generating.

Later, however, after 1979 and 1980, the Japanese started to bring their budgetary position closer to balance. Their investment rates also declined somewhat. So these two things, the decline in their investment and the tendency of their government now to borrow less, were manifested in this higher trade surplus abroad.

The CHAIRMAN. Gentlemen, thank you very much. We will stand in recess for about 10 to 15 minutes until we get back from voting.

[Whereupon, at 12:01 p.m., the hearing was recessed.]

AFTER RECESS

The CHAIRMAN. The committee will come to order, please.

We conclude with Mr. Calvert, Mr. Harrington, and Mr. Conner.

Mr. Calvert, why don't you go right ahead? As I have indicated to the other witnesses, your entire statements will be in the record, and if you could abbreviate them we would appreciate it.

STATEMENT OF D.W. CALVERT, CHAIRMAN, AGRICO CHEMICAL CO., TULSA, OK, A SUBSIDIARY OF THE WILLIAMS COS.

Mr. CALVERT. Thank you, Mr. Chairman.

My name is D.W. Calvert. I am vice chairman of the Williams Cos., and the chairman of Agrico Chemical Co., a wholly-owned subsidiary.

Agrico produces nitrogen and phosphate fertilizers in the United States. We also own a 25-percent equity interest in a South Korean fertilizer complex.

I appreciate your invitation to be here today. My remarks will focus on what is fair and unfair in competition between private producers and state-owned enterprises.

As a producer of nitrogen and phosphate fertilizers, Agrico has been uniquely positioned to witness, since 1970, the shift of Government ownership and control of the majority of global nitrogen and phosphate fertilizer production. Today, only 11 percent of nitrogen fertilizer production and 14 percent of phosphate fertilizer production remain in private hands outside the United States. A similar shift of government majority ownership is taking place in the oil refining business.

The United States has decontrolled oil and most natural gas. Canada is also decontrolling energy. We strongly support these actions, but we are competing in a world in which most governments exercise total control over oil and natural gas production and sales and have established state ownership and control in the downstream production of fertilizers, petrochemicals, and refined petroleum products.

I also wish to emphasize that the United States has had no duties or tariffs on fertilizer imports since 1922, while our exports continue to face such barriers.

In the wake of energy decontrol and the growth in competition with state enterprises, U.S. ammonia producers have encountered new forms of unfair trade. Today we are forced to compete with state enterprises which discriminate in energy and natural resource pricing and ignore market forces. The problem is not what governments do in their own economies, but the effects of their discriminatory policies when they engage in world commerce. Certain governments create an artificial production cost advantage for their own energy-intensive industries. This artificial advantage also causes the construction of excess capacity which is not justified by demand.

Our main production cost in producing ammonia and urea is natural gas, which accounts for 70 to 80 percent of our cash manufacturing costs. Most U.S. producers pay in the range of $2.50 to $2.75 per million BTU's for their natural gas. At the current price of ammonia on the U.S. gulf coast, the value of the natural gas in Soviet ammonia is estimated to be a negative 89 cents per million BTU's. In Soviet urea it is estimated to be a negative $1.36 per million BTU's. Mexican import prices also indicate low or negative natural gas values.

I have a copy of this cost analysis and information on import levels for inclusion in the record.

[The information follows:]

1985 MEXICAN AND U.S.S.R. AMMONIA AND UREA GAS NETBACKS
$/Metric Ton

	Mexico		U.S.S.R.	
	Ammonia	Urea	Ammonia	Urea
U.S. Gulf Price (1)	$123.50	$100.00	$123.50	$100.00
Less Shipping (2) (Loading Port)	15.00 (Cosoleacaque)	10.00 (Cosoleacaque)	32.00 (Yuzhny)	20.00 (Odessa)
Net Back Port	108.50	90.00	91.50	80.00
Less Inland Transportation	-	-	25.00 (3)	15.00 (3)
Net Back Plant Gate (Plant)	108.50 (Cosoleacaque)	90.00 (Cosoleacaque)	66.50 (Gorlouka)	65.00 (Severodonetsk)
Less Manufacturing Cash Cost	18.00	26.40 (4)	18.00	26.40 (4)
Less Debt Service (5)	56.00	56.50	56.00	56.50
Gas Value @ Plant	$ 34.50	$ 7.10	$ (7.50)	$(17.90)
$/MMBTU Equivalent	$ 0.86	$ 0.26	$ (0.19)	$ (0.66)
Less Pipeline	0.15	0.15	0.50	0.50
Less Gathering	0.20	0.20	0.20	0.20
Wellhead Gas Value	$ 0.51	$ (0.09)	$ (0.89)	$ (1.36)
Memo Usage MMBTU Per Ton	40.0	27.2 (6)	40.0	27.2 (6)

(1) Green Markets 11/18/85
(2) Based on BSC reported charter rates 3/85-6/85 for similar movement
(3) Based on cost of similar U.S. movement over like distances
(4) (18.00 x .58) + 16.00
(5) Debt service
    NH_3 $165MM for 385M TPY or $430/MT capital cost; 10 year debt service @ 10% on 80% of total ($56.00/Ton NH_3)
    Urea $120MM for 660M TPY or $180/MT capital cost; 10 year debt service @ 10% on 80% of total [$24.00/Ton urea + (.58 x $56/Ton NH_3)] = $56.50
(6) (.58 x 40) +4 = 27.2

P3OPL.26/24

CONDITIONS FACING U.S. DOMESTIC NITROGEN PRODUCERS: THE TROUBLE IS NOT OVER

Prepared by the Ad Hoc Committee of Domestic Nitrogen Producers

The opinion of some U.S. government officials -- that the U.S. nitrogen fertilizer industry's decline has abated and that normal conditions for the industry are returning -- is without basis. In fact, current developments presage another period of intense turmoil. Four key factors are involved: 1) increasing imports of low-priced urea from non-market economies (NMEs) -- the Soviet Union, Romania and East Germany; 2) the likelihood that some form of large U.S. farm acreage set-aside programs will be adopted next year, reducing nitrogen fertilizer demand; 3) a cutback in urea purchases by nations traditionally supplied by U.S. exports, such as China and India; and 4) the probability that new Middle Eastern and North African production will influence traditional U.S. export markets in Eastern Asia and the Mediterranean. These factors could create a situation equivalent to or worse than that experienced during the PIK program in 1983.

Conditions facing the industry led a Chase Econometrics analyst to tell a seminar of fertilizer analysts that U.S. producers should consider pulling out of the domestic market. Chase Econometrics agricultural director Ray Daniels, quoted in Green Markets (10-14-85), described the fertilizer business as one of "risk management for the next six months to two years...In 50 years of dealing with agriculture we've never seen one of these problems." He estimated that agribusinesses will probably have to write off "at least two-three percent of their accounts receivable" in 1985 and that the farm credit system will lose some $6 billion in bad debts.

Massive harvests this year in conjunction with falling grain values and reduced U.S. exports will create untenable surpluses. Chase Econometrics believes that the government will have to sponsor a 30 percent set-aside program on corn next year. Bills before Senate Agriculture already contemplate wheat and corn acreage reductions. Wheat and corn production are directly related to nitrogen application. According to Chase, farm programs calling for 15-20 percent acreage reductions for corn and 20-30 percent for wheat will result in decreased nitrogen demand of 755,000-1 million short tons. Chase put farm nitrogen consumption in 1984 at 11.3 million short tons.

If these demand reductions ensue, the nitrogen price declines of the PIK farm program will again occur. If, as in 1983, domestic producers cut back production and importers don't cut back supply, the domestic industry will experience severe financial difficulty and more U.S. capacity will be closed.

Minimal or negative returns since 1982 have put domestic producers in a weaker position going into this period than they enjoyed in the period before the PIK disruption. While natural gas prices to many U.S. nitrogen producers have declined, U.S. ammonia and urea prices have declined even further, and are again producing substandard or negative margins for U.S. producers.

Blue, Johnson & Associates, a consulting firm specializing in fertilizer and energy, reports that U.S. producers' ratio of net income to total assets before interest and taxes (for basic integrated producers, from Fertilizer Institute data, adjusted to exclude the bias of old, low-cost gas contracts) was 4.9 percent in 1981, -4.5 percent in 1982, -3.9 percent in 1983, 1.2 percent in 1984, and an estimated -2.5 percent in 1985. The brief improvement in 1984 may be attributed to an increase in U.S. nitrogen demand from domestic producers as the PIK program ended and Mexican ammonia imports declined dramatically.

However, negative returns over the next two years, resulting from intensified import competition in the face of reduced domestic demand, will result in the loss of more U.S. nitrogen capacity. The results of previous losses are reflected in the continuing decline of U.S. nitrogen capacity since 1982 and increased reliance on imports (see Charts 1, 2 and 3).

According to Blue, Johnson & Associates, wholesale ammonia prices in the U.S. fell by 18 percent from Spring 1981 through Spring 1983, while farm gate prices fell by 3.5 percent. Thus, the margin for distributors and dealers increased. Prices for major crops were also declining. During this time, U.S. ammonia producers experienced a $13 per ton increase in average production costs due to rising U.S. gas prices. Gas prices to domestic ammonia plants are now around $3.00 mmBTU. A few producers still purchase natural gas for less than $1.00 mmBTU, and a few pay over $3.75 mmBTU.

The U.S. industry continued to operate at high utilization rates through the first half of 1985. High utilization rates, however, must be viewed in relation to the loss of approximately 2 million tons of domestic production capacity since 1982. In order to maintain market penetration next year if demand declines in response to acreage reductions, imports will have to undercut domestic prices. This is already occurring, particularly in urea. Undercutting was used during the entry of Soviet and Mexican ammonia into the U.S. market in 1978-1979, and again during the period of the 1983 PIK program.

Despite more favorable gas prices, higher utilization rates and a slight decrease in imports in fertilizer year 1985 vs. 1984, U.S. ammonia and urea prices are at their lowest point in years. Ammonia is selling for $120-$130 per ton on the Gulf Coast, and urea prices quoted last week in Green Markets "ranged from $90-$96/st FOB [Gulf] for imports, with most in the range of $92-$95/st." These price declines can be attributed to a rapid loss of export markets in the second half of 1985 and, at the same time, an increase in urea imports from NME suppliers.

The problem faced by the U.S. nitrogen industry since 1978 has been increasing competition from state-owned energy and fertilizer enterprises. When demand, prices and U.S. industry operating rates are high, the problem seems to vanish; but when demand falls due to set-aside programs or low expected returns on grain prices, imports produced with lower-priced natural gas continue to enter the country in increasing volumes despite depressed selling prices.

An analysis done by Agrico Chemical Company reveals that government ownership and control of world nitrogen production facilities reached 77 percent in fertilizer year 1984-1985. If U.S. capacity, over 99 percent privately-owned, is netted out of the world total, only 11 percent of world nitrogen production is now carried out by private industry. The only other private concentration is in Canada. While West Germany also has privately-held production, it is important to note that Kuwait has taken an ownership position in West German nitrogen fertilizer production and is bringing in ammonia produced in Kuwait to process in West Germany.

The U.S. marketplace cannot establish a floor price that reflects market-based production costs, due to the availability of imports produced with natural gas held below market value by foreign government pricing policies or practices. As a result, U.S. producers have been forced to sell below their fully-allocated costs and even below their direct cash production costs to retain customers and market share. U.S. producers cannot continue to sell below their direct cash costs without the loss of more capacity.

The nitrogen import problem now centers on urea imports. The relationship between ammonia and urea production and profitability is of critical importance to U.S. and other market-based producers. Urea, produced using ammonia, is a higher value-added product and has generated a greater return per unit sold. For the last several years, urea has returned a price differential of roughly 6 - 7 cents more than ammonia, based on nitrogen content per pound of product. Urea is produced most efficiently and cost-effectively on site at ammonia facilities, where urea trains can utilize by-product CO2 streams from ammonia production trains.

Trend analysis demonstrates that urea imports, both in tonnage and as a percentage of total nitrogen imports, have increased in the 1980s (see Chart 4). As urea imports have increased, the percentage penetration of other nitrogen-based imports has declined. This trend indicates that urea as a percentage of total nitrogen imports will continue increasing. If acreage reduction programs are adopted over the next two years, this change will have a profound impact on U.S. production capacity for both ammonia and urea.

As previously indicated, the price of urea imports has been falling while imports of urea have increased. The United States currently has enough urea capacity to meet domestic needs. However, some of this capacity has been idled recently by low-priced imports. In addition, Canadian urea plants have closed down recently due to very low urea prices in the U.S. market. These low prices are the result of increased urea imports from the Soviet Union, Romania and East Germany (see Chart 3). These nations are the price undercutters.

In addition, the historic price differential between ammonia and urea has changed, not just on the Gulf Coast, but inland in areas such as the Midwest. This directly affects farm decisions on whether to use ammonia or urea. As the price of urea falls, it becomes more attractive in relation to ammonia. While the nitrogen content of urea is lower per pound than that of ammonia, ammonia is more expensive to apply than urea. Ammonia application requires spraying machinery, while urea can be applied by hand or with less expensive equipment.

Low urea prices have moved from the Gulf Coast to other regions, such as the Midwest. If the price differential falls into the range of 3 cents, farmers will be more inclined to use urea because the higher cost of applying ammonia to the soil will negate the ammonia's price advantage differential. In order to sell ammonia, producers and marketers will be under pressure to reduce ammonia prices. This would occur even as urea prices firmed under increased demand.

Industry sources in the Midwest report that low-priced imports in the Gulf are exerting downward pressure on urea prices. Green Markets reports that urea prices in the Mid Corn Belt are now $113 - $137 per ton. At the upper end of this price range, the differential between urea and ammonia is only about 4.5 cents per pound of nitrogen content. An analysis based on historical differentials would indicate, for example, that if urea prices in the Midwest were to remain at around $125 per ton, ammonia prices in the Midwest would have to fall to around $150 per ton from the current price of about $175 to maintain the current differential of about 4.5 cents. If ammonia prices in that region remained at their current level of $175 per ton, the nitrogen content price differential would decline to under 3 cents from the current differential. Because most U.S. regional prices are based on Gulf Coast prices plus transportation and terminal charges, this would put further downward pressure on Gulf Coast prices and returns to nitrogen producers.

An example of this process is:

The nitrogen content of a short ton (2,000 pounds) of ammonia is 1,640 pounds. The nitrogen content of a short ton of urea is 920 pounds.

In Spring 1984 FOB Midwest, ammonia was priced at $210 per ton, or $.1280 per pound of nitrogen content. Urea was priced at $185 per ton, or $.2011 per ton of nitrogen content. The differential between the price of the nitrogen content in urea minus that of ammonia was as follows:

$$\begin{array}{r} \$.2011 \\ -\underline{.1280} \\ \$.0731 \end{array}$$

If low priced imports on the Gulf depress urea selling prices in the Midwest to $125 per ton while the price of ammonia is $175 per ton, the differential produced as urea minus ammonia would decline as follows:

$$\begin{array}{r} \$.1359 \\ -\underline{.1067} \\ \$.0292 \end{array}$$

CHART 1

U.S. AMMONIA CAPACITY
PRODUCTION, CONSUMPTION
AND TRADE
1970 - 1985

(000 Short Tons Nitrogen)

YEAR	U.S. AMMONIA INDUSTRY		U.S. AMMONIA CONSUMPTION			U.S. AMMONIA TRADE		
	CAPACITY[1]	PRODUCTION[2]	FERTILIZER	OTHER[3]	TOTAL[4,5]	EXPORTS	IMPORTS	NET EXP. (IMP
1970	13,040	10,870	7,459	2,873	10,332	1,594	900	694
1971	13,679	11,420	8,134	3,201	11,335	1,206	964	742
1972	13,785	12,070	8,022	3,942	11,964	1,122	883	239
1973	13,674	12,792	8,295	4,092	12,387	1,511	954	557
1974	13,758	12,854	9,157	3,703	12,860	1,278	1,143	135
1975	14,172	12,294	8,601	3,978	12,579	1,126	1,285	(159)
1976	14,844	13,596	10,412	3,332	13,744	1,248	1,276	(28)
1977	15,562	13,987	10,647	4,205	14,852	1,258	1,997	(739)
1978	17,014	13,719	9,965	4,096	14,061	1,811	2,041	(230)
1979	16,445	14,475	10,715	4,006	14,721	2,489	2,314	175
1980	16,504	15,827	11,407	4,602	16,009	2,659	2,730	(71)
1981	16,604	16,071	11,924	3,752	15,676	3,107	2,622	485
1982	16,214	14,445	10,983	3,757	14,740	2,502	2,717	(215)
1983	15,228	11,658	9,127	3,440	12,567	2,039	2,883	(844)
1984	14,830	12,834	11,146	3,868	15,014	2,043	4,127	(2,084)
1985	14,636	13,900	ND*	ND*	ND*	3,228	3,859	(631)

*Estimates: no finals till November

NOTES

ALL NUMBERS BY FERTILIZER YEAR (ending June 30)
1 ton ammonia = .82 tons nitrogen.

1. Total production capability basis 340 days operation at design daily capacity.

2. Gross U.S. ammonia production netted for change in producer inventories of anhydrous ammonia and converted nitrogen products.

3. Other use includes industrial use, process losses and unaccounted disappearance.

4. Total use includes by-product nitrogen, i.e., ammonia liquor and coke oven ammonium sulphate and phosphate, and natural organic material used as fertilizer.

5. Production + Net Exp. (Imp.) + By-Product = Total U.S. Consumption.

CHART 2

U.S. AMMONIA IMPORTS
BY SUPPLIER BY QUARTER AND YEAR
1981 - JULY YTD 1985
(000 Short Tons Nitrogen)

		1981					1982				
		1 Q	2 Q	3 Q	4 Q	TOTAL	1 Q	2 Q	3 Q	4 Q	TOTAL
1)	Canada	63,394	77,922	130,546	128,852	400,714	102,150	98,211	154,942	120,892	476,195
2)	Mexico	59,872	46,962	142,231	122,460	371,525	136,516	121,890	137,012	104,092	499,510
3)	Trinidad/Tobago	69,743	70,758	104,612	46,416	291,529	50,383	71,838	42,814	73,907	238,942
4)	Fr. West Indies	7,720				7,720	7,778				7,778
5)	Neth. Antilles	7,377				7,377			19,569		19,569
6)	Venezuela									17,137	17,137
7)	Brazil										
8)	Colombia										
9)	Bahamas										
10)	Dom. Republic										
11)	Chile										
12)	Jamaica										
13)	Netherlands		1			1					
14)	France									5	5
15)	West Germany										
16)	USSR	229,267	129,107	121,072	174,360	653,806	175,728	130,746	75,977	113,888	496,339
17)	Taiwan										
18)	Jordan										
19)	Italy										
	TOTALS	437,373	324,750	498,461	472,088	1,732,672	472,555	422,685	430,314	429,921	1,755,475

		1983					1984		
1 Q	2 Q	3 Q	4 Q	TOTAL	1 Q	2 Q	3 Q	4 Q	TOTAL
87,843	159,330	186,783	206,955	641,111	216,222	186,617	209,808	137,963	750,610
86,715	105,828	83,791	195,767	472,101	51,144	118,204	54,556	44,491	268,395
97,208	96,508	139,650	106,052	439,418	152,529	152,559	171,217	135,258	611,563
	39,621		17,582	57,203	33,854				33,854
9,050	14,253			23,303	29,315	12,407			41,722
					17,249	36,205			53,454
	4,755	2,722		7,477					
	21	269	53	343	32	38	39	74	183
					4,302				4,302
					2,625				2,625
						38	2		40
								7,238	7,238
					5,430				5,430
130,301	69,101	91,491	236,593	527,486	223,303	167,526	184,486	108,569	683,884
		1		1					
					16				16
411,117	489,617	504,707	763,002	2,168,443	736,021	673,594	620,108	433,593	2,463,316

		1985		
1 Q	2 Q	3 Q	4 Q	TOTAL
198,587	218,547	65,204		482,338
28,294	23,831	9,299		61,424
105,215	107,099	21,606		233,920
	36,214			36,214
		38		38
38				38
		264		264
1				1
213,598	145,128	45,694		404,420
19,582	45,051	9,680		74,313
565,315	575,870	151,785		1,292,970

CHART 3

U.S. UREA IMPORTS
BY SUPPLIER BY QUARTER AND YEAR
1981 - 1985 YTD JULY
(000 Short Tons Nitrogen)

		1981					1982				
		1 Q	2 Q	3 Q	4 Q	TOTAL	1 Q	2 Q	3 Q	4 Q	TOTAL
1)	Canada	113,317	80,435	46,698	59,783	300,233	81,861	80,199	59,002	65,035	286,097
2)	Trinidad/Tobago	1,394	2,644	3,987		8,025	2,656	5,103	4,500	1,334	13,593
3)	Venezuela	319	2,754			3,073		5,831			5,831
4)	Mexico								15	79	94
5)	Fr. West Indies			1,356		1,356	1,378				1,378
6)	Brazil										
7)	Neth. Antilles										
8)	Netherlands		8,113	2,665	42,095	52,873	21,324	29,949	43,662	30,593	125,528
9)	United Kingdom			10		10		1			1
10)	Austria		8			8	8	8			16
11)	West Germany	3	1		1	5	1	3	1	6,444	6,449
12)	Ireland							8,968	8,322		17,290
13)	Norway						2,760				2,760
14)	Finland										
15)	Belgium/Luxem.										
16)	Italy										
17)	Qatar			8,692	10,875	19,567					
18)	Libya										
19)	Israel										
20)	New Zealand										
21)	Hong Kong										
22)	Romania		7,333			7,333					
23)	East Germany						5,578				5,578
24)	USSR						16,298		10,056	18,252	44,606
25)	Japan										
26)	China										
27)	South Korea										
28)	Gabon										
29)	Cayman Islands										
	TOTALS	115,033	101,288	63,408	112,754	392,483	131,864	130,062	125,558	121,737	509,221

1983 2 Q	1983 3 Q	1983 4 Q	1983 TOTAL	1984 1 Q	1984 2 Q	1984 3 Q	1984 4 Q	1984 TOTAL
81,600	53,709	90,881	352,146	123,109	96,435	74,433	64,753	358,730
			3,926	3,640		3,952		7,592
20,760		10,235	66,586	22,158	8,605		5,286	36,049
325	17,813	15,994	34,275	15,327	308	205	159	15,999
5,350	1,328		7,965					
6,759			15,944					
	2,637		2,637					
26,570	18,314	2,277	70,085	12,508	25,859	3,549	11,134	53,050
					4			4
			8			2		2
5	8	6	139	29,379	3	1	1	29,384
	1,760	5,570	8,710	7,986		1,610		9,596
	918		918					
		507	507	7,837				7,837
					10,648		7,986	18,634
			31,980					
					1,415			1,415
	21		21					
4,431		5,151	9,582		9,963			9,963
							1	1
34,493	6,883	21,227	62,603	32,344	48,755	34,986	46,393	162,478
				11,155		2,536	1,445	28,142
23,415	39,118	46,827	178,011	89,363	59,833	15,055	20,852	185,103
339	52		391		98			98
04,047	142,561	198,675	846,434	354,806	261,926	136,329	171,016	924,077

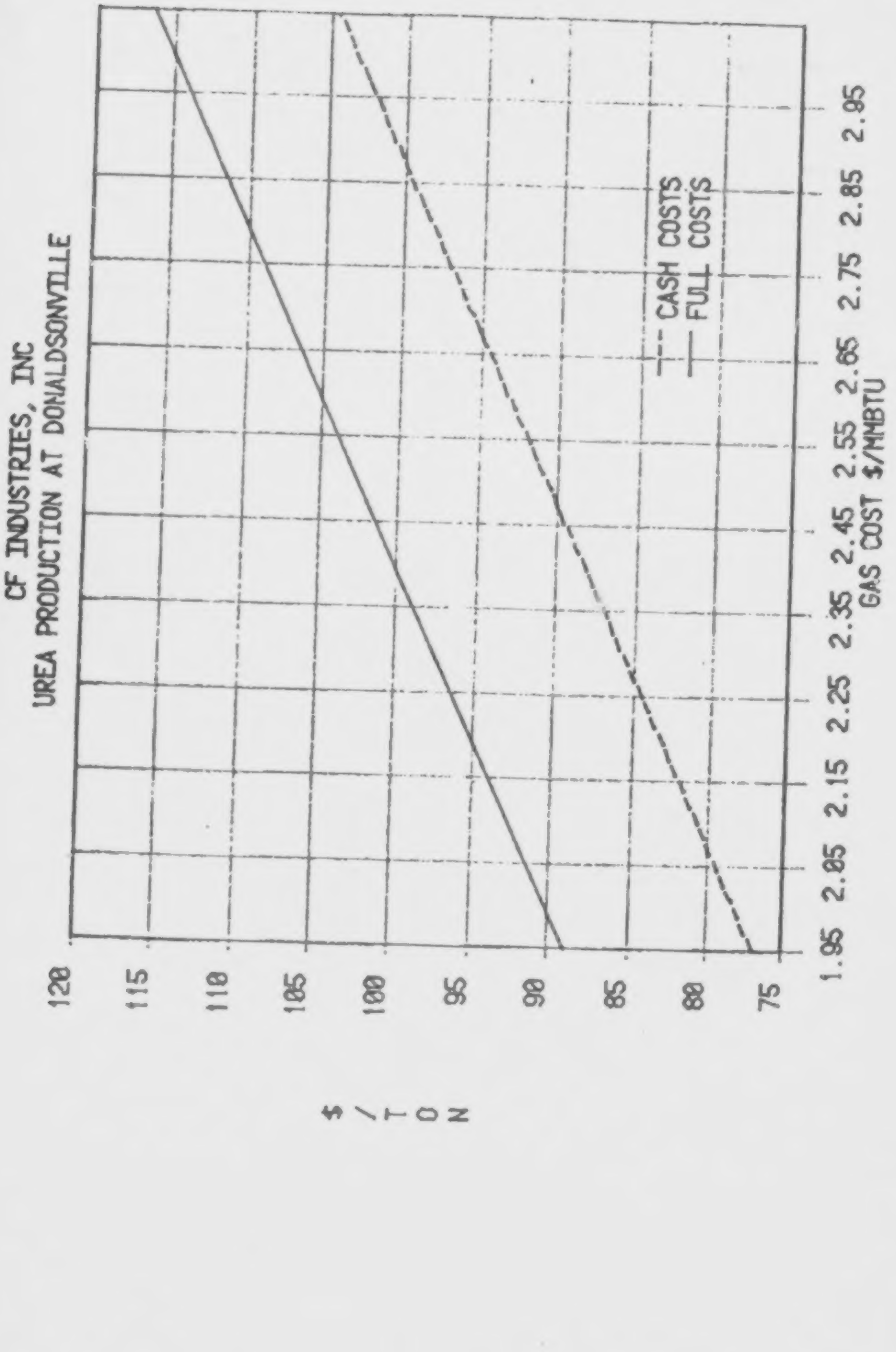
		1985		
1 Q	2 Q	3 Q (July)	4 Q	TOTAL
85,354	133,747	15,070		234,171
8,196	5,225			13,421
348	174	281		803
19,989	20,016	4,318		44,323
3	10,887	1		10,891
	1,940			1,940
19,315	20			19,335
	6,351			6,351
8,027	8,822			16,849
26,649	33,232	12,221		72,102
64,039	57,382			121,421
18	54	8		80
8				8
	4			4
229	3,790			4,019
6,352				6,352
238,527	281,644	31,899	N/A	522,070

CHART 4

U.S. IMPORTS OF AMMONIA AND UREA
1981 - 1985 YTD JULY
CALENDAR YEAR
(000 Short Tons Nitrogen)

	AMMONIA		UREA		OTHER	TOTAL
	Volume	%	Volume	%		
1981	1,732,672	68	392,483	15	17	2,553,000
1982	1,755,474	67	509,221	19	14	2,636,000
1983	2,168,443	63	846,434	25	12	3,433,000
1984	2,463,316	58	924,077	22	20	4,228,000
1985 YTD July	1,292,970	66	522,070	27	7	1,951,000

Rounded %
Calendar Year



CF INDUSTRIES, INC
UREA PRODUCTION AT DONALDSONVILLE

Market Watch

UNITED STATES

NITROGEN

Ammonia--Transammonia last week confirmed it is shipping another 9,500 mt out of the US yet this month (see International report), bringing confirmed exports to about 112,000 mt for Nov.-Dec.

The shipments should help stabilize the US market until next year, but prices are still not firm as inclement weather in the Midwest all but dashes hopes of such movement there this season.

Green Markets erred last week. The Smolnyy, to be brought into the country before the end of the year by Occidental, carries 25,000 mt.

Agrico has closed its 1,000-1,100 st/d ammonia plant at Blytheville AR indefinitely due to excess inventories, which reportedly has forced the Peabody Coal Co., supplied by part-owner Agrico, into the spot market.

Other than that, few transactions were reported. For sales that took, prices were at the same levels as the previous week, with barge sales confirmed at the $114-$115/st level. Export prices are said to be somewhat lower, at $110-$113/st.

Urea--Trading in urea was somewhat active last week as traders importing or trying to import product hussled for sales while buyers jockeyed for position either in next spring's market or the current import market.

Prices remained at about the same levels as previously reported, but were weakening slightly. Sales of barges of imported material were made at levels of $89-$90/st FOB Gulf. Among shipments still to come into the Gulf this year are the following:

Company	Ship	Arr.	Quant.	Origin
Mitsui	Maria Sitinas	11/15	25K	Rumania
W&D	Debby	11/17	23K	USSR
Clarendon	Golden Prince	11/22	30K	Rumania
Phibro	Peter Tomasevich	11/22	27.5K	USSR
Mitsui	Prof. Kostyukov	11/25	38.4K	USSR
Phibro	(unknown)	11/27	15K	USSR
Vitol Buck	Golden Star	late-Nov.	25K	Rumania
Cargill	(two vessels)	Nov.	40K	USSR
Kaichem/ Interep	(unknown)	Nov.-Dec.	25K	Rumania
Windmill	Nordic Trader	12/1	16.2K	Ireland
Cargill	(two vessels)	Dec.	40K	USSR
W&D	(unknown)	Dec.	23K	USSR
ContiChem	(unknown)	Dec.	20K	USSR
Total			348.1K	

In addition to this list, Thyssen reportedly was still talking about trying to bring a vessel in from Rumania, probably about 20,000 mt, and probably in December.

Transnitro unloaded 13-14,000 mt of granular product from NSM of the Netherlands at Maumee OH last week after discharging 6,000 mt at an undisclosed eastern Canada location. The company says it may bring about 20,000 mt more product into the Gulf yet this year, which could come either from Qatar or Rumania.

As the imports continued to line up, Agrico confirmed last week that it has shut down its 1,000 st/d urea plant at Blytheville AR indefinitely for inventory control. The plant has been alternately in and out of operation for the past few weeks.

An analyst for the company estimates that producer shipments in the US this fall will be off 10-20% from the approximately 2 million st moved last fall.

PHOSPHATES

DAP--Trading activity was very light in the US last week, with buyers not willing to pay more than $144/st and sellers wanting $148/st. One analysis put together by Agrico estimates that DAP-MAP movement will be down 20% this fall from the 2.8 million st shipped by producers in the US last fall, when movement was slightly higher than the 10-year average.

POTASH

Canadian manufacturers are beginning to announce shut-down plans to relieve the overburden of inventories. IMC is closing both its mines at Esterhazy for three weeks from Dec. 21 through Jan. 31. Some 800 workers will be laid off in that move.

Cominco expects to shave some 100,000 mt of production (product tons) by closing its Vade mine Nov. 9-25 and Dec. 20-Jan. 5. That closure will involve furloughs for 317 employees.

PCS is also planning to shut down production of all mines from about Dec. 20 through Jan. 5 for a loss of about 75,000 mt.

MIDWEST

Hopes for further fall fertilizer movement are waning as rain and snow continue to fall. It appears that virtually no work has been done in the fields at all since the storms began around Veteran's Day.

Reports of four inches of rainfall in a five-day period were not uncommon, and dealers in Nebraska reported as much as 7 inches of snow. Forecasts predict more of the same for the next few days.

When farmers are again able to get into the fields it is expected that they will concentrate on bringing in the remainder of the harvest. In most areas few soybeans remain in fields, but across the region only 80-85% of the corn is in.

Dealers report that fall movement is significantly off from last year, and most are sitting on adequate stocks. There is a general feeling that product could be had for less than the asking prices if one were ready to make a purchase. Those who could be enticed to buy if the terms were right say they are holding out for offers with price protection. These dealers feel that such offers will not be long in coming as wholesale sales are almost at a standstill.

One dealer in Illinois reported that he has a railcar of DAP scheduled to arrive soon, the result of a purchase made a couple of weeks ago when product was moving. This sale, at about $168/st DEL, and another small purchase made at $180/st FOB Omaha NE would indicate, that prices have not yet softened in response to the slow movement over the last weeks.

NORTHWEST

Fertilizer prices are continuing to slide in the Pacific Northwest. As a result, dealers say they won't fill up their "empty sheds" until January or February, unless they sense earlier that the market is bottoming out and it would be wise to buy.

But dealers also believe that spring wholesale prices will go beyond reflecting the supply of products. They say demand will enter into pricing

Mr. CALVERT. Soviet and Mexican plants employ the same technology as our plants in the United States; their plants are more expensive to construct, however, and operate less efficiently. In addition, Soviet fertilizer producers must pay to transport their products some 6,000 miles to reach U.S. markets.

The continued penetration of our marketplace by imports produced and traded in this manner will cause a shutdown of more efficient U.S producers. This means the loss of jobs and investments in the United States to unfair trade. If U.S. producers lose money, we must shut down. These state-owned enterprises do not. It is more important for them to maintain production and export sales in order to generate hard currency and jobs.

The GATT makes it clear that governments should not discriminate among producers or establish discriminatory practices which distort and disrupt world trade. GATT article XVII, quoted on page 6 of my written testimony, says that governments should act "solely in accordance with commercial considerations" and "in accordance with customary business practice" when they compete with private sector producers in trade. This principle of nondiscrimination is already imbedded in U.S. law. Under the U.S. General System of Preferences, equitable and reasonable access to the markets and basic commodity resources of nations are criteria for eligibility. This principle has been part of U.S. law for over 10 years; but, by definition, it does not apply to OPEC nations or nonmarket economies. Virtually all U.S trade laws have proven inapplicable to these cases.

We support the legislation introduced by Senators Baucus and Long, Senate bill 1292, which already addresses the natural resource problems I have described. Their legislation would give U.S. producers their day in court to prove the existence of these natural resource distortions and gain relief under our countervailing duty laws.

Thank you, sir, and I will be glad to answer any questions.

The CHAIRMAN. Thank you, sir.

Mr. Harrington.

[Mr. Calvert's written testimony follows:]

ABSTRACT OF THE TESTIMONY OF D.W. CALVERT
CHAIRMAN OF AGRICO CHEMICAL COMPANY
BEFORE THE
SENATE FINANCE COMMITTEE

Trade Policy Hearings
November 21, 1985

- President Reagan, in his recent trade policy statement, said, "I believe that if trade is not fair for all, then trade is 'free' in name only."

- Fair trade exists when producers compete by the same rules. Unfair trade exists when specific forms of discrimination cause injury to otherwise competitive producers; this occurs when governments or producers bend the rules in their favor in a discriminatory, inequitable fashion.

- Unfair trade among nations is occurring in the area of energy and energy-intensive product trade. The proliferation of state energy enterprises using discriminatory practices has caused new problems for U.S. private producers of energy and downstream energy-intensive products.

- While the United States and Canada have deregulated oil and most natural gas, the governments of other nations continue to exert control over energy resources. Increasingly, this control extends to ownership of the industries which use those resources and the enterprises which market their products.

- Some governments pursue energy and natural resource development policies in which market considerations are not predominant. These governments discriminate in the pricing of and access to natural resource inputs to production in favor of their own industries. This in turn causes unwarranted increases in exports, decreases in imports, and provides a measure of protection in their home markets.

- Government discrimination in access and pricing of natural resources may also distort the investment decision. It leads to excessive investments in plant and equipment which are uneconomic, and which are not justified by demand either in the domestic market or in foreign markets. Such investments then require continued subsidies to maintain operations and product sales at lower prices in oversupplied export markets.

- State enterprise and state trading are not unfair *per se*. When state enterprises operate with due regard for commercial considerations in the marketplace, the potential for market distortion is minimized.

- GATT Article XVII on "State Trading" makes it clear that state enterprises should act "solely in accordance with commercial considerations" and "in accordance with customary business practice."

- We are approaching a crossroads. Our trade laws must be modernized to deal with with the non-market practices encountered in direct competition with government-owned or controlled enterprises in the U.S. and third country markets. If the U.S. Government does not act, the U.S. will be forced to sacrifice private sector competitiveness in those markets.

TESTIMONY OF D.W. CALVERT
CHAIRMAN OF AGRICO CHEMICAL COMPANY
BEFORE THE
SENATE FINANCE COMMITTEE

Trade Policy Hearings
November 21, 1985

Mr. Chairman and Members of the Subcommitee:

My name is D.W. Calvert. I am Vice-chairman of The Williams Companies and Chairman of the Board of Agrico Chemical Company, a wholly-owned subsidiary. Agrico is a member of the Ad Hoc Committee of Domestic Nitrogen Producers, a coalition of seven major U.S. nitrogen producers with facilities located in the United States and overseas.

Agrico is a major producer of nitrogen and phosphate fertilizer products in the United States. We also own a 25 percent equity interest in a major fertilizer complex in South Korea. Our export sales of $261 million in 1984 accounted for over 30 percent of our total sales. We are also importers. We have overseas offices in Seoul, Hong Kong, Paris, the Cayman Islands and Trinidad.

We appreciate this opportunity to discuss what constitutes fair and unfair trade practices. This is the central, pragamatic issue that must be clarified in the current trade debate. President Reagan, in his recent statement on international trade policy, said, "I believe that if trade is not fair for all, then trade is 'free' in name only." I agree with the President, but what we need is action, not just words. Generally, "free trade" is an economic theory. It is based on the concept of efficiency. It requires open markets among all trading nations in order to work and provide its benefit. The United States is committed to an open market trading system in the world, but it suffices to say that there is no such market system in the real world. It remains a goal.

"Fair trade" is a political-economic standard based on the concept of equity. It denotes the idea that, in the absence of free trade, competing producers should be given equal treatment by governments and play by the same ground rules in the world marketplace. "Unfair trade" arises when there is some form of discrimination which causes injury to an otherwise competitive industry; it occurs when governments or producers bend the rules in their favor or ignore them entirely.

Fair trade is equitable. Unfair trade is inequitable.

Fair trade is non-discriminatory. Unfair trade is discriminatory.

Fair trade is the exercise of a natural or comparative advantage. Unfair trade is the exercise of a contrived or artificial advantage.

My testimony will focus on what is fair and unfair trade in energy and energy-intensive products like fertilizers and petrochemicals. That is the business I know and deal in every day. I intend to point out what is fair and unfair trade in relation to direct competition with state enterprises because, increasingly, they are the entities with whom we compete in trade with energy resources, fertilizer, petrochemicals, refined petroleum products and other energy intensive products. I submit that we will never achieve fair trade between U.S. producers and government producers in these interrelated industries if the U.S. does not provide trade policy leadership. The U.S. should require market-oriented practices by all participants in energy product trade. The U.S. government must act to identify and offset the most disruptive non-market actions of foreign government enterprises in these industries.

The Congress is endeavoring to develop a balanced U.S. trade policy that will promote an open trading system and provide remedies to eliminate or offset the effects of unfair trade practices. The problem is defining what is unfair. Regarding trade in energy and natural resource-based products, the increasing dominance of state enterprises and the use of discriminatory pricing and access restrictions on natural resources must be addressed decisively. The U.S. International Trade Commission's report # 1696 on natural resources investigated pricing policies and practices used by foreign governments. The report revealed the widespread use of discriminatory pricing for natural resources.

New rules of the game must be developed to address these developments. Otherwise, these discriminatory practices will continue to be extended into the downstream production of fertilizers, petrochemicals and other resource-intensive products. World trade will suffer dramatically if these practices of state enterprises continue to expand as a rule and do not decline as a transitory exception. When discriminatory economic practices of a foreign government provide a contrived competitive advantage for its producers which injures competing producers, that is unfair trade. Discrimination is the key.

In a sense, we are approaching a crossroads. If the United States is to retain a healthy and competitive private sector in energy and natural resource-intensive industries, our trade laws must be modernized to address the downside of direct competition against governments. We should not allow competitive, efficient private producers to be sacrificed to the discriminatory practices encountered in the increasing competition with state-owned and controlled enterprises. The alternative is to follow the lead of some of our trading partners and engage in direct industrial policy control or even government support of major energy-related segments of our economy -- or we may have to return to energy regulation and controls in the not-too-distant future, in order to offset oligopolistic prices and market control by foreign government producers and cartels. I don't think that the American people or the people in this room would favor either alternative.

UNFAIRNESS IN WORLD ENERGY TRADE

The Williams Companies are engaged in the energy business. We are involved in natural gas and petroleum pipelines, oil and gas production, coal production and commercial real estate, in addition to the chemical fertilizer business.

The United States has moved toward reliance on market forces for energy pricing and trade in the 1980s by decontrolling oil and deregulating most previously-regulated natural gas. We strongly support this policy. Canada is also deregulating energy. It must be noted, however, that the United States and Canada are becoming, for all intents and purposes, a free market island in world energy trade. Most governments have opted to continue to exert a major direct influence in their nations' energy marketplaces.

Most of the world's oil supplies are in nations where the government owns and controls production of crude oil, as are most of the world's reserves of natural gas. As these government-owners have moved downstream into the production of refined products, petrochemicals and other energy-intensive goods, the conditions of competition have changed dramatically. Private producers are confronting closed markets, preferential financing, subsidies, and overall increased competition from government-owned and controlled companies.

As an energy and chemical enterprise engaged in domestic production and sales, foreign production, and exports and imports, we have observed first-hand a significant shift from private ownership to state ownership and control in the production of oil and gas and other natural resources. This shift is also evident in the downstream utilization of these resources in the production of fertilizers, petrochemicals and refined petroleum products.

Since the 1970s, world ammonia production has shifted from private ownership to government ownership and control. Today, 77 percent of the world's ammonia is produced by governments. Outside of the United States, only 11 percent of ammonia production is in private hands. Regarding phosphate fertilizer production, 38 percent was government-owned in 1970. Today, 56 percent is government-owned. Outside the United States, only 14 percent is in private hands. According to Energy Economics, October 1984, a publication of the Chase Manhattan Bank, the addition of new OPEC refineries this year will push the government ownership of petroleum product refining capacity to over 50 percent of the Free World's total capacity. If the non-market economies of the Communist nations are included, the government ownership ratio is much higher.

State enterprise and state trading per se are not unfair trade practices. To the extent state enterprises operate with due regard for commercial considerations in the marketplace, potential distortion is minimized. However, with direct involvement in the production and sale of energy and natural resources, as well as the downstream production, marketing and sale of goods made from those resources, some governments have developed policies and practices which result in discriminatory pricing and access to natural resources. By doing so, they have created a contrived, artificial advantage for their industries in international trade. Such governments have increasingly erected tariff and non-tariff barriers, provided government financing at below-market rates to build excess production capacity not justified by market demand, and have restricted both pricing and access to natural resources in their countries. Many of these policies and practices have been justified as necessary to foster their economic development. These governments also pursue policies in which market considerations are not the predominant factors.

Many of these governments have blurred the distinction betweeen commercial enterprise and the pursuit of economic, social and political development objectives. They have used the monopoly power of government ownership and control to discriminate in favor of their industries and to promote exports by those industries. Private producers utilizing private capital must receive a reasonable return on their investment in the marketplace, and cannot compete with monopolistic government enterprises which discriminate in their commercial practices. Making a profit is not always the primary objective of government-owned enterprises.

Governments should be allowed to manage the use of their countries' natural resources to develop their domestic economies. The GATT makes that abundantly clear. But the GATT also makes it clear that nations should not unfairly discriminate among producers or establish discriminatory practices which disrupt or distort world trade. Governments are not permitted to provide export or domestic subsidies which injure producers of their trading partners. GATT Article XVII addresses "State Trading Enterprises." Paragraph 1(b) reads as follows:

> The provisions of sub-paragraph (a) of this paragraph shall be understood to require that such enterprises shall, having due regard to the other provisions of this Agreement, make any such purchases or sales [e.g. imports and exports] solely in accordance with commercial considerations,* including price, quality, availability, marketability, transportation and other conditions of purchase or sale, and shall afford the enterprises of the other contracting parties adequate opportunity, in accorance with customary business practice, to compete for participation in such purchases or sales. [emphasis added]

Sub-paragraph (a) basically says that governments should act, in trade matters, in a "non-discriminatory" manner toward private traders. The GATT rule on State Trading makes it clear that the GATT intended that governments should not use their potential monopoly power to disadvantage private sector competitors.

The concept of equitable and reasonable access to the markets and basic commodity resources of other countries is expressly set out in the criteria under U.S. law for eligibility under the Generalized System of Preferences (19 U.S.C. 2462(c)(4)). Communist countries and OPEC countries are generally not eligible for GSP, however, and these countries are some of the worst offenders in energy and product trade. They are also generally not members of GATT. Thus, there are few if any direct sanctions or rules that apply to trade in these sectors with such countries under GATT, GSP or other U.S. law.

U.S. countervailing duty and antidumping laws, as well as Section 337, have proven inadequate to deal with these practices. Section 201 and Section 406 sanctions have been inconsistently applied by the President and are essentially useless in resolving trade conflicts in these industrial sectors. Section 301 has been suggested as a possible remedy, but its use and remedies are totally discretionary with the President. The Administration has yet to indicate a willingness to use Section 301 to address the practices I have described.

I believe that the U.S. must exert leadership in reforming its trade laws and international trading rules to deal with these discriminatory practices. The objective must be to allow the marketplace -- not governments -- to set prices and access to energy and natural resources used in production. Commercial considerations in the marketplace must be the standard for investment in plants that manufacture such products.

THE SITUATION FACING FERTILIZER PRODUCERS

As a nitrogen fertilizer producer, Agrico must compete against government fertilizer enterprises which are owned or controlled by government companies. Our major concern is obtaining natural gas at the best available price, because natural gas is the main component of ammonia and its most expensive input, representing 70 to 80 percent, or more, of cash production costs. We have the same concerns for pricing and access to phosphate rock to make phosphate fertilizers. Oil, gas and coal are the basic feedstocks and energy sources for the production of petrochemicals, refined products, asphalt and cement, to name a few. If governments do not allow fair and equitable pricing and access to these natural resources, based on market-oriented criteria, unfair trade in goods manufactured from these resources is the inevitable result.

Conditions in the nitrogen fertilizer market have been worsening quickly over the last several months. The price of ammonia, the basic nitrogen fertilizer, has fallen to 1983 PIK program levels of $120 per ton or less on the U.S. Gulf Coast. The price of urea, a nitrogen fertilizer made from ammonia, has fallen to its lowest point in years -- imports from Romania, East Germany and the Soviet Union have driven the Gulf Coast price for this commodity down into the $90 per-ton range. U.S. producers are struggling to recover their direct cash production costs. At these prices, recovering full production costs is out of the question for many producers. Some U.S. producers, including Agrico, have been forced to close down their plants in the last few weeks. Canadian urea plants have also shut down due to price depression and lower demand in the U.S. market.

According to Blue, Johnson & Associates, a consulting firm specializing in fertilizer and energy, U.S. nitrogen producers' ratio of net income to total assets before interest and taxes (adjusted to exclude the bias of old, low-cost intrastate gas contracts which are rapidly expiring and account for less than 10 percent of U.S. ammonia production) was 4.9 percent in 1981, -4.5 percent in 1982, -3.9 percent in 1983, 1.2 percent in 1984 and an estimated -2.5 percent in 1985. The brief improvement in 1984 may be attributed to an increase in U.S. nitrogen demand for domestic producers as the PIK program ended and Mexican ammonia exports to the U.S. were cut back dramatically.

Today, U.S. fertilizer producers may be on the verge of their worst period ever. Two factors will play key parts in the fertilizer business over the next two years. First, the ongoing problem of disruptive and unfair trade practices of certain government-owned fertilizer operations overseas will continue to plague the domestic industry. Second, there is a strong move afoot to adopt acreage reduction programs for next planting season. An acreage reduction of 20 - 30 percent for corn and wheat, in combination with low-priced imports which continue to enter our market regardless of market conditions, would result in another period of devastation for the U.S. ammonia industry.

The U.S. ammonia industry has lost capacity every year since 1981 for a net reduction of over 2 million tons, a loss of about 11 percent of our total capacity. The worst period prior to the one we're looking at now was during the 1983 PIK program, when U.S. farmers reduced their nitrogen consumption in response to acreage reduction incentives. U.S. nitrogen producers responded to the demand decline by shutting down some plants and drastically curtailing production at remaining facilities. However, imports continued to increase. The end of the PIK program left the United States more dependent on imports and with a reduced nitrogen fertilizer production capacity.

Chase Econometrics agricultural director Ray Daniels, at a recent seminar, described the fertilizer business as one of "risk management for the next six months to two years." He said, "In 50 years of dealing with agriculture we've never seen one of these problems." Mr. Daniels explained that acreage reduction programs of the scope anticipated would reduce U.S. farm demand for nitrogen fertilizers by about one million tons. He predicted that agribusiness would have to write off "at least 2 - 3 percent of their accounts receivable" and that the farm credit system would lose some $6 billion in bad debt. You are, no doubt, aware that this figure could reach $10 billion.

If this acreage reduction comes about, I can tell you what will happen. U.S. nitrogen fertilizer producers will curtail production in an attempt to balance supply with demand and to maintain prices even at their current depressed levels. I would call this a "market-based response to market conditions." But imports from the non-market economies and other government-owned fertilizer operations overseas will continue at their surging levels. Prices will fall further -- below the cost of production for virtually all U.S. producers. Another round of permanent U.S. plant closures will ensue, and imports will gain greater penetration of the U.S. market, as they have done at a steady pace since the early 1980s. In other words, we'll rerun the 1981-1983 scenario. I would call this "market disruption."

If these state enterprises were operating "solely in accordance with commercial considerations," to quote the GATT, then imports would be drastically reduced as well. But if our experience of the last few years repeats itself, those imports will increase both relatively and actually. That increase in market share during a period of depressed demand can only be accomplished by unfair trade practices. A few foreign producers enjoy a comparative advantage in nitrogen fertilizer production. Most do not relative to the United States. This latter group -- all state-owned producers -- should drop out of the market. But I can assure you that they will not. They will continue to employ their unfair advantages and shut down some of our plants in the process.

UNFAIR TRADE PRACTICES THAT AFFECT U.S. FERTILIZER PRODUCERS

Conventional Tariff and Non-tariff Barriers

World trade in fertilizers is very important to our industry and our country. This past fertilizer year, over 11 million tons of upgraded phosphates were exported. This represented over half of upgraded phosphate production in the United States and was worth about $1.75 billion.

However, there are a number of import barriers and unfair trade practices which put U.S. fertilizer producers at a disadvantage. These barriers are protectionist in the narrowest sense; that is, while not bestowing direct aid on a government's industry, these barriers reduce competition in the home market. These include import duties, import quotas and/or licenses, countertrade or bilateral trade requirements. Then there are less conventional unfair trade practices -- those involving pricing and access controls on natural resource inputs. Subsidies can take myriad forms, but I will discuss the two which seem most serious to U.S. producers: direct financial subsidies and natural resource subsidies.

On the subject of tariff and non-tariff barriers, the U.S. industry faces discrimination on several fronts. The EEC imposes import duties, based on the landed value of the product, ranging from 4.8 to 13.2 percent on phosphate fertilizers and 8 to 11.7 percent on nitrogen fertilizers. This practice by the EEC is completely unwarranted and unfair. The U.S. does not have similar duties on imports of nitrogen products from the EEC. During 1984, imports of these products from the EEC had a total declared value of about $45 million. It is difficult to pinpoint the business potential for U.S. companies if the EEC abolished its duties. I believe that, conservatively, U.S. companies could ship 300,000 tons of ammonia, urea and solutions to the EEC with a total value of $50 million if these duties were abolished.

There are also duties which are imposed to discriminate only against exporters of a certain country, often the United States. For example, the EEC imposes an import duty of 11.7 percent on urea, a solid form of nitrogen fertilizer. This is true for urea that originates from the U.S. or Eastern Europe. However, if it comes from our competitors in the Middle East or the Third World, it is essentially duty-free. The import duty on diammonium phosphate (DAP) from the U.S. is 6.6 percent, while DAP from our major world competitors in Morocco, Tunisia, South Africa and Jordan enters the EEC duty-free. These are but a few examples of the discriminatory application of import duties.

I need to emphasize that the United States has no duties on any type of fertilizer from any source. The U.S. has had no duties or tariffs on fertilizers since 1922. To address this inequity, the U.S. fertilizer industry strongly supports new multilateral trade negotiations where the U.S. could press for elimination of both tariff and non-tariff barriers to fertilizer trade. However, some industry members have pointed out that, because we do not have any restrictions, it may be hard to bargain for the reduction of restrictions overseas.

The second major impediment that I want to bring to your attention is that of the import quota and license. Import licenses are required by nearly all Latin American countries. Again, it is difficult to quantify the impact on U.S. exports. However, we believe that if import licenses and duties were abolished in Brazil alone, U.S. exports of fertilizer would increase by 500,000 metric tons with a value in excess of $100 million.

A third and growing impediment can be found in countertrade or bilateral trade requirements. Some foreign governments are requiring that foreign sellers of products buy back an equivalent monetary amount of goods from the importing country. For instance, India has announced new rules that stipulate the fertilizer suppliers who sign long-term agreements will be expected to take back Indian goods valued at 50 percent of fertilizer sales by 1986. This will increase to 75 percent in 1987 and 100 percent in 1988. In some cases, the foreign government will not accept barters unless they are handled through other government entities. U.S. fertilizer companies have found it necessary to sell to foreign government companies which then finalize the barter agreements. This form of barter trade is a step backwards in international commerce. On any significant level, such trade could result in the disruption of the prices of the bartered commodities. It must be closely observed in order to assure that it does not become a major hindrance to U.S. producers.

NATURAL RESOURCE SUBSIDIES: THE MAJOR DILEMMA

The trade barriers I have discussed so far are conventional in scope and require conventional responses. But there are unconventional trade barriers of greater impact which arise from direct competition with state enterprises. These are the problems associated with discriminatory intervention in natural resource pricing and access by governments. As I have explained, two concerns are foremost. First, government discrimination in resource pricing and access can lead to investments in plant and equipment which are uneconomic and which are not justified by demand. Second, this intervention requires an ongoing production cost subsidy for resource-intensive producers in the government-assisted industry.

Natural Resource Subsidies Distort the Investment Decision

The construction of a world-scale ammonia plant requires a huge capital expenditure, in excess of $200 million in the United States and more in countries with less favorable capital costs and infrastructure development. Analyses by the United Nations Food and Agriculture Organization and the World Bank have made it plain that the United States is a very attractive investment site for new plants to supply U.S. demand and has been for several years. What these analyses do is compare all the factors of production -- materials, capital and labor -- in relation to the country's existing infrastructure to support the new plant, and then arrive at a realization price which would justify the investment. According to these analyses, the cost of producing ammonia and urea in the U.S. is competitive with or better than many of our state-owned competitors' costs in terms of supplying the U.S. market. Advantages in capital costs, infrastructure costs and transportation costs for U.S. producers serve to offset the advantage of low-cost gas in remote locations and less-developed country locations.

However, these analyses are based on real economic costs incurred and a return on investment. We face competition from nations where the state energy enterprise, not the marketplace, determines energy prices and whether investments are to be made in production facilities. This investment decision need not be demand-driven. Once such a plant is built, it will be run regardless. Neither must it provide a return comparable to that which a private producer would require from a major investment. Thus, we face competition from state enterprises that desire to sell all their production at whatever price they can get, even if it does not recover all production costs or provide a return on investment. As you know, there are foreign competitors in the U.S. market less concerned with return on investment than with generating hard currency to repay their debts.

In order to continue operations and make their plants competitive, governments must often provide the natural resource inputs at very low or even zero cost. The Indonesian government is constructing a $350 million methanol plant on Bunyu Island despite the methanol glut that has existed for years on world markets. The Commerce Department calculated that the natural gas input cost to this plant would have to be less than zero in order to make it in any way competitive.

The Soviet Union undertook a major expansion of its ammonia capacity in the mid-1970s, surpassing the United States as the world's largest producer by 1980. Soviet plants, based on netback prices from the U.S. Gulf Coast, are apparently receiving natural gas at very low cost -- well below the apparent price in hard currencies of Soviet gas sold to Western and Eastern European customers. This was substantiated in the recent ITC study I referred to previously.

There are also instances where a government and private parties contract together to build plants. This kind of arrangement may well be the wave of the future for U.S. companies wishing to make investments overseas. It is not always the most efficient use of capital or in the best interests of the United States, because it still may distort the investment decision and move more U.S. plants offshore. In Thailand, the government-controlled National

Fertilizer Corporation has been trying to build an ammonia plant using about two-thirds private financing and one-third government financing. Numerous problems have delayed the plant, and the government is trying to increase its capitalization. As reported in Green Markets, the weekly fertilizer newspaper, an executive of the Bangkok Bank said NFC's capital should not be increased. 'This is a political project with a very high risk rate,' he said. 'We consider it an unfeasible project.'" Government-private joint ventures have been undertaken successfully in some countries, not so successfully in others. While such ventures can work to the benefit of both the developing country and the private joint partner if based on sound commercial considerations, they may also work to change and distort trade if based on subsidized capital and energy feedstocks provided at less than market value. The latter category of plant should not be built. It will result in unfair trade, excess supply and will shut down more efficient producers.

If such plants are built, the subsidies should be offset -- countervailed -- and such plants should be forced to operate on an equal economic basis. If they cannot survive without subsidies then they should be shut down, allowing more efficient producers to remain in the market.

Natural Resource Subsidies Provide Unfair Production Cost Advantages

Instead of seeking profit, such government operations seek political objectives and the hard currency that exports earn in foreign markets. We hear over and over that governments are not required to profit-maximize. Many take the view that they do not need to make a profit or return on investment at all, or capture the opportunity cost of their natural resources. If governments are engaging in state enterprise, why should they be allowed to invest, produce and sell under a different set of economic rules or "fair trade" rules?

State enterprise or government-supported plants, once up and running, need not respond to market conditions of oversupply in export markets. They may simply continue to lower their prices in those markets to ensure that their production is sold. When demand drops they may continue to run their plants at full capacity. These two factors disrupt commodity pricing mechanisms of the marketplace. In commodity markets, the incremental unit sets the price -- even an offer of sale at a lower price can affect the market's pricing. Government-subsidized producers have no real production cost floor in relation to private, market-based producers. When prices fall below the cash production cost of manufacturing the product in the U.S. market, U.S. producers cover their losses as long as they can and then shut down. When push comes to shove, it is very probable that government-supported plants will outlast private producers who must seek capital from private institutions. Government-owned plants do not go bankrupt or shut down. They are further subsidized and continue to operate.

It is also important to note that many of these countries require labor-intensive industries for balanced economic development. Instead, they divert scarce capital into capital-intensive industries that provide few jobs, little or no return on investment, and little or no return on the real economic value of their natural resources. Value-added is not captured because these plants end up selling excess product into an oversupplied market, lowering all prices and producing economic losses. None of the anticipated economic benefit flows back into that country's economy. Capital is wasted that could have been devoted to more beneficial uses. Debt repayment ability is also reduced.

The fertilizer industry has encountered serious problems with imports into the United States of ammonia and urea from the Soviet Union, Mexico and Eastern Bloc countries like Romania. In these countries, nitrogen fertilizer production is reserved for the government energy and petrochemical sector. These government producers charge themselves artificial, below-market prices for the natural gas used in making ammonia and urea in their plants. Both the Soviet Union and Mexico have exported natural gas for much higher prices determined by export market prices, while providing their own industries with the same raw materials at much lower prices. Yet under current trade laws, these blatantly unfair, protectionist acts may go unremedied.

I have heard these government programs defended as simple exercises of "comparative advantage." Like "free trade," this has become another well-meaning but badly-abused term.

In some cases, governments -- even state enterprises -- are exercising their comparative advantage and not discriminating. The pricing of and access to natural gas used to make fertilizer and petrochemicals in Trinidad and Saudi Arabia are examples. These countries cannot export natural gas competitively because in order to export they would have to first liquify the gas. This expensive process would render their natural gas exports uncompetitive. They have generally allowed equitable investment by foreign companies and equal marketing control by the private partner. They appear to receive the fair market value for their natural gas and have not discriminated in their pricing. These joint ventures have, by and large, been arms-length transactions, operated with due regard for commerical considerations. Imports from the plants in these countries can thus be presumed to be traded fairly, absent other more conventional unfair trade practices. The same cannot be said for Mexican policy or in general for Eastern Bloc policy. David Ricardo would roll over in his grave to hear government discriminatory pricing systems and government-restricted access to critical resources defended under his theory of comparative advantage.

I believe that the U.S. Government must take active steps to eliminate discrimination in natural resource pricing and access by foreign governments, and thereby allow U.S. companies to participate on an equal footing with foreign competitors. A trade policy based on non-intervention and reliance solely on the marketplace to eliminate this type of discrimination will fail. Private producers with private capital cannot stay in the game long enough for the market to overcome these practices. In that sense -- only in that sense -- we cannot compete. We should strive for a "fair trade" system where everyone is playing by the same rules. Too often, we have allowed significant penetration of our markets by countries that will not give us a fair shot at their markets or raw materials. We must insist on fair access to markets and raw materials overseas. We must prevent subsidized or unfair penetration of our market.

Thank you. I would be very pleased to answer any questions you have.

STATEMENT OF W. BRENDAN HARRINGTON, PUBLIC AFFAIRS REPRESENTATIVE, CARGILL, INC., WASHINGTON, DC

Mr. HARRINGTON. Thank you, Senator.

I am Brendan Harrington, a public affairs representative of Cargill, Inc., and I also serve as chair of the Coalition to Promote America's Trade.

My company has been active on behalf of agricultural interests, individually and as a member of the PAT Coalition, in opposing natural resource legislation.

We do understand that the Trade Subcommittee plans to hold more indepth hearings on this legislation later on; but, for the purposes of today's hearing, it provides an especially good illustration of the costs, especially for agriculture, of many of the trade measures now receiving attention in Congress.

Let me first clarify that Cargill does have a parochial interest in natural resource legislation. However, by far our greater concern is over the many harmful ways in which natural resource legislation, if enacted, would affect U.S. agricultural exports.

This legislation would expand the scope of U.S. countervailing duty laws to impose duties on imports of a wide range of products simply because they are produced from low-cost natural resources in foreign nations.

In general, under the GATT a government may confer a benefit, including low-cost inputs, on its industry. However, the price of the benefit must not be below its cost to the government, and the benefit must be generally available—that is, not targeted to a particular industry or to exports.

Natural resource legislation was designed originally to affect Mexico. As now drafted, however, the several bills before Congress would reach far beyond that country, and in effect attempt to dictate internal pricing decisions to our trading partners.

The price of enacting natural resource legislation will be high, especially for U.S. agriculture. Wharton Econometrics estimates enactment of this legislation will cost some 345,000 jobs over the next 5 years, while creating only 8,000 new jobs. U.S. farm income alone would be reduced by some $24 billion over that time.

Now, economists and other experts may quibble over methodologies and assumptions, but the Wharton figures undeniably show a clear trend.

U.S farmers will suffer as countervailing duties establish a price floor for fertilizer inputs higher than the prevailing world price, increasing U.S. grain prices at a time when U.S agricultural exports are already down some 27 percent from 1981. Moreover, it is highly likely that countries whose exports are affected by new duties will retaliate against U.S exports—agricultural, cheif among them.

It is equally likely that other countries will follow the U.S. lead and enact similar legislation affecting U.S. products.

Finally, it is not unreasonable to expect that U.S. exports of the same goods subject to the new duties will be backed out of the foreign markets as the lower-priced foreign goods, denied access to the U.S. market, seek a home.

Natural resource legislation also fails to address the fundamental cyclical causes of low nitrogen fertilizer prices that originally gave rise to complaints against imports. The domestic nitrogen industry is characterized by volatile swings in demand, influenced by a wide variety of factors affecting fertilizer consumption trends. At one point, for example, the 1982 recession, a severe drought, and acreage reduction under the PIK program all combined to precipitate a roughly one-quarter decline in nitrogen use.

If indeed Congress makes the decision to change the treatment of natural resource cost and pricing advantages, there are certainly other more responsible courses of action to pursue than those under the countervailing duty law.

Although my company does not believe that it is necessary to change current law, multilateral negotiations such as proposed yesterday by members of this committee, or even bilateral negotiations, seem a far more responsible approach than unilaterally imposing countervailing duties to offset a legitimate price/cost advantage.

Finally, natural resource legislation also fails to address the major causes of the Nation's trade deficits, including the Federal budget deficit and the high-valued dollar, the slower rate at which our trading partners are recovering from the recent economic recession, and the critical need of Third World nations to reduce their debt burdens.

Mr. Chairman, I appreciate very much having the opportunity to appear before you today.

The CHAIRMAN. Thank you.

Mr. Conner.

[Mr. Harrington's written testimony follows:]

Statement of W. Brendan Harrington
Cargill, Inc.
Before The
Senate Finance Committee
November 21, 1985

Mr. Chairman and members of the committee, I am Brendan Harrington, a public affairs representative of Cargill, Inc. I also serve as chair of the Coalition to Promote America's Trade (PAT), a broad-based coalition of companies that oppose so-called "natural resource" legislation.

I am here today primarily to express the concern of my company and that of most agricultural interests over proposals before the 99th Congress to enact legislation designed to protect U.S. businesses facing increased foreign competition.

In particular, my company has been active individually and as a member of the PAT Coalition in opposing controversial legislative proposals to impose countervailing duties on imported products that have benefited from low-cost natural resource inputs in their country of origin. It is our understanding that this committee's trade subcommittee plans to hold in-depth hearings on natural resource pricing practices in the near future, and we look forward to participating in those hearings.

However, for the purposes of today's hearing, natural resource legislation provides a good illustration of the costs, especially for agriculture, of many of the trade measures now receiving attention in Congress. In addition, such proposals, including natural resource legislation, both fail to address the problems experienced by particular industries and ignore the real, macroeconomic causes of this country's growing trade deficits.

Let me first clarify that Cargill has a parochial interest in natural resource legislation. Among other fertilizer operations, Cargill is involved in nearly every phase of nitrogen fertilizer importation and distribution and is also a domestic producer.

However, by far our greatest concern is over the many harmful ways in which imposition of countervailing duties under natural resource legislation, if enacted, would affect U.S. agriculture and our agricultural exports.

Natural resource legislation would expand the scope of U.S. countervailing duty laws to impose duties on imports of a wide range products simply because they are produced from low-cost natural resources in foreign nations. Under the bills, countervailable subsidies would arise when a foreign government provides a low-cost natural resource to its local producers of downstream merchandise at prices below some presumed "fair market value" of the resource.

Sponsors of natural resource legislation maintain that the difference between the domestic sales price and that fair market value constitutes an impermissible export subsidy.

In general, under the General Agreement on Tariffs and Trade (GATT), a government may confer a benefit, including low-cost inputs, on its industries. However, the price of the benefit must not be below its cost to the government, and the benefit must be generally available--that is, not targeted to a particular industry or to exports.

Natural resource legislation was designed originally to counteract Mexico's GATT-consistent practice of selling natural gas to domestic consumers, regardless of the purpose for which the domestic consumer used that gas, at a price much lower than it sells gas for export. As now drafted, however, the several bills before Congress would reach far beyond Mexico, as more and more nations, particularly lesser-developed countries seeking to relieve huge debt burdens, seek to add value to their exports.

In effect, the legislation attempts to dictate internal pricing decisions to our international trading partners. If foreign countries export a resource for less than the domestic price, they would be subject to an antidumping action. If the price is higher, then the new countervailing duties would be imposed. That does not leave much flexibility.

The price of enacting natural resource legislation will be high, especially for U.S. agriculture. In its recent study, Wharton Econometrics has projected that in all, enactment of this legislation will cost the U.S. economy some 345,000 jobs over the next five years, while creating only 8,000 new jobs, as a result of increased prices and reduced exports. U.S. farm income alone would be reduced by some $24 billion over that time as a result of higher fertilizer prices and trade actions, according to the Wharton study.

Economists and other experts may quibble over methodologies or assumptions, but the Wharton figures undeniably show a clear trend. Jobs lost would vastly outnumber jobs saved or created under such legislation.

U.S. farmers, in particular, will suffer as countervailing duties establish a price floor for fertilizer inputs higher than the prevailing world price. Higher input prices will inevitably translate into higher grain and product prices at a time when U.S. agricultural exports already are down by 27 percent from 1981.

Moreover, because of the serious GATT implications of such legislation, it is highly likely that countries whose exports are affected by new duties will retaliate against U.S. exports, agricultural exports chief among them.

It is equally likely that other countries will follow the U.S. lead and enact similar legislation, which would affect numerous U.S. products that benefit from government-subsidized hydropower, irrigation, and a host of other practices. The United States itself has long distorted its domestic energy prices through price controls and special tax incentives.

Finally, it is not unreasonable to expect that U.S. exports of the same goods subject to the new duties will be backed out of foreign markets as the lower-priced foreign goods, denied access to the U.S. market, seek a home.

Like other measures, natural resource legislation fails to address the fundamental causes of the problems that the domestic nitrogen fertilizer industry has experienced in recent years. The low nitrogen fertilizer prices that gave rise to complaints against imports stemmed in fact from cyclical, temporary demand factors.

At one point, three major factors combined to reduce demand. The 1982 recession, a severe drought, and acreage reduction under the PIK (payment-in-kind) program precipitated a roughly one-quarter decline in nitrogen use.

Similarly, our fertilizer division reports that prices have been somewhat soft during this year's fall fertilizer season. But questions over acreage setaside programs under the unfinished farm bill and a late harvest--again, cyclical factors affecting demand--are attributed as causes of this price softness.

Moreover, lower natural gas prices--recently as low as $2.00 on the spot market--are serving to bolster the domestic industry, even in face of slack demand.

Thus, the domestic nitrogen industry is characterized in the short run by volatile swings in demand, influenced by a wide variety of factors affecting fertilizer consumption trends. In the long run, a further shift in production capabilities is occurring as new, more efficient plants are coming on line and older plants are being modernized both in the United States and in other countries that desire to utilize better their comparative advantages in abundant natural resources.

Therefore, the countervailing duty approach contained in the various natural resource measures before the 99th Congress is fundamentally inappropriate as a response to the problems faced by the industry that those measures seek to protect.

The unilateral approach to pricing advantages embodied in most current natural resource proposals runs the very real risk of violating our international obligations. If indeed Congress makes the decision to change the treatment of natural resource cost and pricing advantages, there are certainly other, more responsible courses of action to pursue.

One approach, for example, may be contained in the bipartisan

Senate trade package proposed yesterday. According to earlier reports on the proposal, this legislation would direct the president to raise natural resource cost advantages, along with some 10 other issues, in the context of a new round of Multilateral Trade Negotiations.

Although my company, and the other members of the PAT Coalition, do not believe that it is necessary to change the treatment of such pricing practices as they are now permitted under the GATT, multilateral, or even bilateral, negotiations seem a far more preferable approach than unilaterally imposing countervailing duties to offset a legitimate price/cost advantage.

Mr. Chairman, Cargill recently joined a group of 20 agricultural interests on a letter to each member of Congress in opposition to legislation that targets specific countries or specific industries. Natural resource legislation is just such a proposal.

And, like most other trade measures before this Congress, it is unilateral in nature and fails to address both the particular problems being faced by the industry it seeks to protect and the major causes of the nation's trade deficits--including the federal budget deficit and the high-valued dollar; the slower rate at which our trading partners are recovering from the recent economic recession, and the critical need of third-world nations to reduce their debt burdens.

In conclusion, Mr. Chairman, I appreciate very much having the opportunity to appear before you today to express both my company's concerns and those of agriculture in general over efforts to enact legislation to protect various U.S. industries. Natural resource legislation provides but one example of how inappropriate such measures are for the problems they seek to address.

Thank you.

STATEMENT OF JIM H. CONNER, CHAIRMAN, TRADE REFORM ACTION COALITION, WASHINGTON, DC

Mr. **Conner**. Mr. Chairman, I would like to request that our full statement be entered for the record, and I am going to depart from that, if I may.

The **Chairman**. Without objection.

Mr. **Conner**. My name is Jim Conner, executive vice president of the American Yarn Spinners Association, and I appear before you today as chairman of the Trade Reform Action Coalition [TRAC].

TRAC represents a substantial cross section of American companies, trade associations, and labor unions, formed over 2 years ago to support the strengthening and modernization of key U.S trade laws. Industries represented include automobile parts, chemicals, footwear, furniture, leather goods, metalworking, natural and manmade fibers, textiles, apparel, nonferrous metals, steel, and steel distribution.

It is not easy to distinguish between fair and unfair trade, because years of benign neglect of foreign unfair trade practices have left many U.S. industries in such serious distress that they are forced to seek comprehensive solutions to manage trade. Inadequate trade laws and trade-law enforcement are part of the problem.

Since 1980 we have doubled the debt level accumulated over the previous 200 years. Our trade balance has gone from a surplus to what will likely be a record deficit of $150 billion or so this year. As of mid-year we became a debtor nation.

Some economists are predicting that unless the trade deficit is not checked the United States will owe foreigners $1 trillion by 1990.

Our manufacturing base is being eroded by unfair trade practices of foreign nations, our farmers are losing international markets for the same reason and are unable to meet their mortgage payments, as evidenced by the near collapse of the Federal Farm Credit System.

Textbook theory voiced by officials of this administration is in sharp contrast with the real world in which we live today. Foreign nations, both developing and developed, bar our products from their shores, while at the same time demand increased access to our markets in the name of free trade.

Last week you heard the testimony of Ambassador Yeutter when he wrote off large segments of the U.S. economy as expendable. I can assure you that his testimony received wide coverage in industrial-area newspapers across this land, and in my own industry it prompted numerous phone calls from irate manufacturers. The question asked was singly clear:

> How can the administration give lip-service to a fair trade policy while at the same time using every response at its disposal to prevent Congress from acting against unfair trade practices?

It has come to our attention that some in the Congress, having fallen victim to the administration's rhetoric, are questioning whether or not there really is a fair trade problem, or if U.S. industry is just crying for unwarranted protection from foreign competition. To that, I would simply point to the record compiled by the

International Trade Commission, the Office of Compliance in the Department of Commerce, numerous congressional hearings, and more recently the U.S. Trade Representative's compilation of restrictive trade practices of other nations.

I feel fully confident expressing the view that a wide credibility gap exists today between what the administration states as its trade policy and what it practices.

On July 8, 1981, U.S. Trade Representative William Brock appeared before the Senate Finance Committee, and in his testimony he stated, "The administration will strictly enforce U.S. trade laws on international agreements relating to international trade"; if this or previous administrations had lived up to this kind of a commitment, why have only 12 of the 55 escape-clause cases brought under the current statute resulted in import relief for the petitioner? Why was the footwear industry refused relief by the President after receiving a unanimous finding of serious import injury from the International Trade Commission? Why, in spite of commitments made during the Tokyo Round have developing countries been granted the injury test under the Subsidies Code without taking meaningful steps to dispose of their export subsidies?

Why have some countries been given reprieves of as long as 6 years to eliminate their subsidies? Why have countries which reneged on their commitments and then reinstituted their export subsidies been permitted to keep the injury test? Why do we continue to allow Japan to maintain quotas that are illegal under the GATT without retaliation? Why do we tolerate trade restrictive practices by other GATT members while at the same time bending over backward to justify the lack of enforcement of GATT rules on behalf of our own industries?

We were sorely disappointed to learn earlier this week that a major bipartisan trade bill was introduced that, unlike S. 1493, excluded important provisions pertaining to reform in the antidumping and countervailing duty statutes. Most of the previous provisions, which are included in S. 1493, overwhelmingly passed both Houses of Congress in 1984 but were dropped in conference at the insistence of the administration.

It is ludicrous to talk about meaningful trade reform without considering changes to the unfair trade statutes. It is our hope that Congress is coming to the conclusion that talk about fair trade is useful only to the extent that it achieves results. To date, we see little to encourage us to believe that our trading partners will act to eliminate unfair trade practices until it is in their best interests to do so.

We, therefore, are of the strong conviction that the United States must act decisively, and now, to avoid further deterioration of our industrial base.

[Mr. Conner's written testimony follows:]

Statement of Jim H. Conner
Chairman
Trade Reform Action Coalition

Summary

TRAC represents a substantial cross-section of American companies, trade associations, and labor unions, formed over two years ago to support the strengthening and modernization of key U.S. trade laws. Industries represented include automotive parts, chemicals, footwear, furniture, leather goods, metalworking, natural and man-made fibers/textiles/ apparel, non-ferrous metals, and steel and steel distribution.

It is not easy to distinguish between "fair" and "unfair trade", because years of benign neglect of foreign unfair trade practices have left many U.S. industries in such serious distress that they are forced to seek comprehensive solutions of managed trade. Inadequate trade laws and trade law enforcement are part of the problem.

We live in a world of managed trade, where the distinction between "fair" and "unfair" trade is often not very clear at all. It is somewhat easier to define trade that is "unfair" than trade that is "fair." Injurious dumping, and foreign government subsidies constitute unfair trade practices. Most would agree that it is unfair when foreign governments "target" their key industries and when they deny reciprocal market access opportunities to U.S. companies. Moreover, there is a growing list of new and more sophisticated types of foreign unfair trade practices.

The question of whether U.S. industries can compete against "fair" trade is an important one. Before we answer "yes", however, we need to ask questions about what is "fair" trade. Is it "fair" that the value of the dollar continues to give an artificial competitive advantage to our foreign competitors? Is it "fair" that most developed nations promote their international competitiveness through highly favorable tax and antitrust policies? Is it "fair" that some foreign industries in the developing world pay their workers bare subsistence wages, with little attention to job standards, safety and a clean environment? Is it "fair" that trade in certain products is increasingly diverted to the U.S. market because other countries have tightly closed their markets?

Regardless of how one answers these questions, one thing seems clear: we need comprehensive trade law reform (1) to make the U.S. "escape clause" (Section 201) a more viable fair trade statute; (2) to make Section 301 a more workable mechanism for responding to foreign unfair trade practices; and (3) to strengthen in key ways our laws against foreign dumping and subsidies. Accordingly, TRAC is supporting the Comprehensive Trade Law Reform Act of 1985 (S. 1493). Much of the content of S. 1493 is not uncharted territory for the Congress, since many of these provisions were adopted in one form or another (by either the House, Senate, or both) by overwhelming margins during the last Congress.

STATEMENT OF

JIM H. CONNER
CHAIRMAN
TRADE REFORM ACTION COALITION

to the

SENATE FINANCE COMMITTEE

on

United States Trade Policy

November 21, 1985

Statement of Jim H. Conner
Chairman
Trade Reform Action Coalition

I am Jim Conner, Executive Vice-President of the American Yarn Spinners Association and Chairman of the multi-industry Trade Reform Action Coalition (TRAC). On behalf of TRAC, I am pleased to be here today to discuss United States trade policy, with particular emphasis on the need for modernizing our trade remedy laws and making them more responsive to U.S. industries.

TRAC represents a substantial cross-section of American companies, trade associations, and labor unions, formed over two years ago to support the strengthening and modernization of key U.S. trade laws. TRAC's member organizations (a listing is attached to my testimony) employ well over 5 million people, and the producing companies account for over $300 billion in annual sales. Industries represented include automotive parts, chemicals, footwear, furniture, leather goods, metalworking, natural and man-made fibers/ textiles/apparel, non-ferrous metals, and steel and steel distribution.

The Trade Reform Action Coalition represents a large slice of American manufacturing, and its member organizations all share two basic concerns: (1) what is happening to our industries because of unfair or disruptive foreign trade practices, and (2) the inability of current trade remedy laws to deal adequately with such practices.

Before I speak to the main issues of this hearing, I would like to give you our view of the current state of U.S. trade policy. Whether "fair" or not, more and more of our industries are being clobbered by international trade. Some economists believe we are merely witnessing a simple shift in "comparative advantage" that is a natural part of the adjustment process. We should not be fooled.

What we are seeing today is the systematic decimation of America's industrial base. One industry after another -- including our most competitive hi-tech industries -- is losing market share as a result of foreign unfair or disruptive trade practices. Our trade deficit was a record $123 billion last year and will probably soar to $150 billion this year.

We have lost about 2 million manufacturing jobs in this country since 1979 alone. These job losses have spanned all manufacturing and have severely impacted some of our most vital industries. They are manufacturing jobs we will never see again. These jobs -- as the President stated recently -- have been replaced by new service sector jobs in the travel industry and in fast food establishments. I submit, however, that a great industrial economy needs more than just service jobs: it requires a sound manufacturing base.

The U.S. economy is today at a crossroads and in dire need of direction. We can continue to pretend that our present trade policy is sufficient, while our trading competitors are destroying our most vital industries; or we can take another path, and that involves re-examining present U.S. trade policy at its roots, and then taking strong action to defend ourselves in what is already a full-scale international trade war -- a war that we are unfortunately losing.

This Committee is taking the first critical step, because it is asking exactly the right kinds of questions: (1) how should fair and unfair trade be distinguished?; (2) can the United States compete with "fair" trade?; and (3) how should the United States respond to foreign "unfair" trade practices? Each of TRAC's member organizations has had to deal with these questions at one time or another from a particular industry perspective, but this hearing asks that we consider these issues from the standpoint of U.S. trade policy in general.

It is often not easy to distinguish between fair and unfair trade, because years of benign neglect of foreign unfair trade practices have left many U.S. industries in such serious distress that they are forced to seek comprehensive solutions of managed trade. Inadequate trade laws and trade law enforcement are part of the problem. However, part of the blame must also go to an incoherent trade policy and the failure to make trade policy a top national priority.

As a result, in recent years we've seen U.S. industries increasingly unsure about which trade statutes to use when filing cases. We've seen Section 301 unfair trade cases turn into Section 201 fair trade cases; and we've seen industries ravaged by pervasive foreign dumping and subsidies file under both Section 201 and Section 301, because these statutes offer at least the possibility of more comprehensive relief. What TRAC's member organizations have learned over the past few years is that we don't live in a world where free trade theory is repeated much in practice and where the line is clearly drawn between fair and unfair trade. We live in a world of managed trade, where the distinction between "fair" and "unfair" trade is often not very clear at all.

Ultimately, it is somewhat easier to define trade that is "unfair" than trade that is "fair." For example, both the GATT and U.S. law recognize that injurious dumping and foreign government subsidies constitute unfair trade practices. Likewise, most would agree that it is unfair when foreign governments "target" their key industries and when they deny reciprocal market access opportunities to U.S. companies. In addition, many now recognize that there is a growing list of new and more sophisticated types of foreign unfair trade practices such as counterfeiting, Customs fraud and patent fraud. It is therefore absolutely essential that we become more aggressive in the actions we take to resolve our unfair trade problem. It's not sufficient, though, since much of our trade problem is not so easily defined.

The question of whether U.S. industries can compete against "fair" trade is an important one. Before we answer "yes", however, we need to ask some more questions about what is "fair" trade. First, is it "fair" that the value of the dollar continues to give an artificial competitive advantage to our foreign competitors? Second, is it "fair" that most developed nations promote their international competitiveness through highly favorable tax and antitrust policies? Third, is it "fair" that some foreign industries in the developing world pay their workers bare subsistence wages, with little attention to job standards, safety and a clean environment? Finally, is it "fair" that trade in certain products is increasingly diverted to the U.S. market because other countries have tightly closed their markets?1/

1/ With respect to this final point, two of TRAC's organizations, the footwear industry and the steel industry, have in the past filed Section 301 petitions alleging that the restrictive practices of various foreign countries have caused "trade diversion" to the U.S. market, but the government's interagency 301 Committee has flatly dismissed these arguments, placing a burden of proof so great on domestic industries that demonstrating a link between the closed markets of our trading partners and increased exports to the U.S. market of the products in question was virtually impossible. For an example of restrictive practices in steel, see the November 1984 Steel Advisory Committee Report, as well as the recent studies on "targeting" by the U.S. International Trade Commission. For an example of restrictive practices in footwear see the

(continued on next page)

In a world in which technology flows fairly easily across national boundaries -- constantly changing relative competitive advantage between countries -- these are not easy questions to answer. Yet, regardless of how one answers these questions, one thing seems clear: we need comprehensive trade law reform (1) to make the U.S. "escape clause" (Section 201) a more viable fair trade statute; (2) to make Section 301 a more workable mechanism for responding to foreign unfair trade practices; and (3) to strengthen in key ways our laws against foreign dumping and subsidies. Accordingly, TRAC is supporting legislation now pending before this Committee that would accomplish these goals. Co-sponsored by Senators John Heinz, Daniel Moynihan, George Mitchell and William Cohen, it is entitled the Comprehensive Trade Law Reform Act of 1985 (S. 1493).

As we saw in the footwear case, our fair trade statute, Section 201, has numerous serious flaws. Decision-making is too politicized. Moreover, the requirement that imports must be the "substantial" cause of injury is over and above what the GATT requires; the "threat of injury" concept is only

---

1/ (continued from previous page) recently revised study by the Department of Commerce entitled Footwear: Tariff and Trade Regulations of Selected Countries that showed that of 53 countries surveyed, 51 have import duties that in some cases are so high as to prohibit imports of footwear; 33 countries impose supplementary taxes or charges and 16 have value added taxes; 34 countries required licenses, maintain quotas or have other restrictions; and 9 countries prohibit all or some footwear.

vaguely defined; petitioners are denied the possibility of early relief if an import surge occurs during the course of an investigation; the law does not allow major parts and component producers to participate in proceedings; and petitioners are prevented from reapplying for relief unless two full years have elapsed. S. 1493 addresses all of these problems. At the same time, it provides for a tighter modernization commitment from petitioning industries as a quid pro quo for more effective relief.

Our Section 301 unfair trade statute is also in need of serious reform. It too is an overly politicized statute; it is lacking in strict time lines; there is often no verification of information submitted by foreign governments; the law has inadequate procedures for disclosure of confidential information; and there is no requirement for action when foreign "targeting" practices cause injury to U.S. companies and workers. S. 1493 addresses all of these problems in an effective and well-reasoned way.

The pervasive nature of foreign dumping and subsidy practices is of particular concern to TRAC's member organizations. Given this level of concern and the more technical nature of U.S. dumping and subsidy law, I would like to take a few extra minutes to cite just four practical examples of the kinds of dumping and subsidy problems our industries are now confronting, and the kinds of solutions to these problems provided for in S. 1493.

First, many dumping and subsidy practices are unreachable under our current trade laws. For instance, while we can take action against directly dumped or subsidized products, there is a gaping loophole in U.S. trade laws regarding unfair trade that is indirect. Current law does not apply at all to dumped inputs that are contained in imports of fabricated products, and existing law only partially reaches inputs that are subsidized. The ultimate effect of foreign fabricated imports containing dumped or subsidized inputs is a severe competitive disadvantage for U.S. producers of competing products.

To close this loophole, S. 1493 makes actionable under the dumping laws, in limited circumstances, the foreign unfair trade practice known as "diversionary dumping" (which both houses of Congress passed in similar form last session). This would allow the Commerce Department to pursue investigations where, for example, Korean steel was sold to a Japanese automobile manufacturer at a dumped price, and the Japanese autos containing this dumped steel were then exported to the U.S. market.

Second, S. 1493 corrects a drafting anomaly in the 1979 Trade Act that has resulted in an unrealistically restrictive interpretation of what constitutes a "countervailable subsidy" (i.e., a subsidy against which penalty duties can be applied). Under current law, penalty duties can only be applied against capital (e.g., loans) made on terms "inconsistent with commercial considerations" (e.g., below market rates) and against the provision of goods or services on "preferential terms" (e.g., on more favorable terms to one industry than to other industries). S. 1493 would eliminate the artificial distinction between subsidized capital and subsidized goods or services. It would do this by allowing penalty duties to be applied against loans made on favorable terms and against the provision of goods or services at below market rates. As a result, if a foreign government provided stumpage payments to its softwood lumber industry at a below market rate, U.S. subsidy law could be applied.

Third, S. 1493 specifies the kinds of commitments to eliminate subsidies that foreign governments should be required to make in order to qualify for (and continue to get) the "injury test" (i.e., the requirement of U.S. industries having to prove injury) under U.S. subsidy law. As Senators Heinz and Danforth have both pointed out, this is necessary, because (1) a number of developing countries have agreed to phase out and end the subsidization of their exports to the U.S market; (2) they have been granted the injury test in exchange; (3) they have continued to subsidize their exports in violation of their commitments; and (4) they have still continued to get the protection under U.S. law afforded by the injury test in subsidy cases. S. 1493 would require that developing countries phase-down and eliminate export subsidies promptly; that the President review compliance on an annual basis; and that the injury test benefit be withdrawn in the event of non-compliance.

Fourth, S. 1493 deals with the serious problem of import surges that frequently occur in the months before or after a petition is filed. Often times a foreign producer will flood the U.S. market with imports just before a case is filed or immediately thereafter in the mere anticipation of the imposition of an offsetting duty on its dumped or subsidized imports. These surges can be devastating to a domestic firm waiting for a remedy to be imposed. Under current law, such surges may be dealt with by findings of "critical circumstances" -- findings that allow for the imposition of retroactive penalty duties. However, in practice, this rarely happens. S. 1493 would establish specific guidelines and timetables to facilitate "critical circumstances" findings in worthy cases.

There are a number of other very important dumping and subsidy provisions in S. 1493 that I would be happy to discuss if we had more time. I have, however, attached a three-page plain English summary to my testimony giving real world examples of how each of these changes would improve current law, and I have also included a section-by-section analysis that describes these changes in detail. In all, Title I of S. 1493 contains 10 essential changes to U.S. dumping and subsidy law. Taken as a whole, they do two important things: (1) they broaden the accessibility of our unfair trade laws to industries that are now denied relief because the laws are either too narrowly defined, or are interpreted and administered in such a way as to limit their applicability; and (2) they provide more predictability and fairness as to how these laws will be administered.

To summarize our view, we believe that some of the tools of a more effective U.S. trade policy can be found in S. 1493. It is a bill that simplifies, expedites and makes more effective the procedures for relief from both unfair and disruptive foreign trade practices under U.S. laws. It is a bill that recognizes that, while some slight progress was made toward these goals with passage of the Trade and Tariff Act of 1984, much more needs to be done.

In sum, S. 1493 is vital legislation, because it takes a giant step toward the achievement of truly effective trade remedy laws; several of the key legislative changes incorporated in S. 1493 have the support of other major private sector groups and many members of Congress; and much of the content of S. 1493 is not uncharted territory for the Congress, since many of these provisions were adopted in one form or another (by either the House, Senate, or both) by overwhelming margins during the last Congress.

Before I end my formal remarks, we would all do well to remember that Article 1, Section 8 of the Constitution states that Congress shall regulate commerce with foreign nations. In practice, Congress has delegated much of the authority for the management of our trade affairs to the President over the years. However, our trade affairs are not being managed well when the trade deficit is at record levels; when industries, such as the footwear industry, are being ravaged by imports, but denied import relief by the President; and when industries, such as the semiconductor industry, are being seriously harmed by foreign unfair trade practices. We therefore believe it is time for Congress to reassert its constitutional powers in this area, and we appeal to you to start this process with the provisions incorporated in S. 1493.

On behalf of all member organizations of TRAC, I appreciate the opportunity you have given me to testify.

July 26, 1985

TRADE REFORM ACTION COALITION (TRAC)

Alliance of Metalworking Industries
Amalgamated Clothing and Textile Workers Union
American Apparel Manufacturers Association
American Brush Manufacturers Association
American Chain Association
American Cutlery Manufacturers Association
American Die Casting Institute
American Federation of Fisherman
American Fiber, Textile, Apparel Coalition
American Furniture Manufacturers Association
American Gear Manufacturers Association
American Institute of Steel Construction, Inc.
American Iron and Steel Institute
American Metal Stamping Association (Washer Division)
American Mushroom Institute
American Pipe Fittings Association
American Textile Machinery Association
American Textile Manufacturers Institute
American Wire Producers Association
American Yarn Spinners Association
Anti-Friction Bearing Manufacturers Association
Automotive Service Industry Association
Association of Die Shops International
Association of Synthetic Yarn Manufacturers
Bicycle Manufacturers Association of America, Inc.
Brass and Bronze Ingot Institute
Carpet and Rug Institute
Cast Iron Soil Pipe Institute
Cast Metals Federation
Clothing Manufacturers Association of America
Committee on Pipe and Tube Imports
Copper and Brass Fabricators Council, Inc.
Cutting Tool Manufacturers Association
Expanded Metal Manufacturers Association
Footwear Industries of America, Inc.
Forging Industry Association
Group of 33
Hand Tools Institute
Industrial Fasteners Institute
Industrial Perforators Association, Inc.
International Ladies' Garment Workers' Union
International Leather Goods, Plastics and Novelty Workers Union
Investment Casting Institute
Iron Castings Society
Knitted Textile Association
Lead-Zinc Producers Committee
Luggage and Leather Goods Manufacturers of America, Inc.
Man-Made Fiber Producers Association, Inc.
Metal Cutting Tool Institute
Metal Treating Institute
Metalworking Fair Trade Coalition

National Association of Chain Manufacturers
National Association of Hosiery Manufacturers
National Association of Pattern Manufacturers
National Association of Uniform Manufacturers
National Cotton Council of America
National Foundry Association
National Knitwear Manufacturers Association
National Knitwear and Sportswear Association
National Screw Machine Products Association
National Tooling and Machining Association
National Wool Growers Association
Neckwear Association of America
Non-Ferrous Founders' Society
Northern Textile Association
Outdoor Power Equipment Institute
Plumbing Manufacturers Institute
Scale Manufacturers Association, Inc.
Steel Founders' Society
Steel Plate Fabricators Association, Inc.
Steel Service Center Institute
Synthetic Organic Chemical Manufacturers Association
Textile Distributors Association, Inc.
Tool and Die Institute
United Food and Commercial Workers International Union
U.S. Fastener Manufacturing Group
Valve Manufacturers Association
Welded Steel Tube Institute
Work Glove Manufacturers Association

S. 1493

THE COMPREHENSIVE TRADE LAW REFORM ACT OF 1985

Title I - Improvements in Antidumping and Countervailing Duty Laws

This Title does the following:

- It makes actionable under Antidumping law, in certain circumstances, the foreign unfair trade practice of "diversionary dumping" (similar to the "upstream dumping" amendment passed by both houses of Congress last year). The provision would only apply where an existing Antidumping order or other arrangement is in effect. This would allow the Commerce Department to pursue investigations where, for example, Korean steel was sold to a Japanese automobile manufacturer at a dumped price, and the Japanese autos containing this dumped steel were then exported to the U.S. market.

- It expands the coverage of "upstream subsidies" under the 1984 Trade Act to subsidies paid or authorized by a customs union or member state, and strengthens the law where the input is subject to an existing CVD order or other arrangement. This would allow the Commerce Department to pursue investigations on a British fabricated product where, for example, the "upstream" subsidy on the input was paid or authorized by the French government.

- It allows companies and workers who make major components (which are intended to be incorporated into final products) to file and participate in Antidumping and Countervailing Duty proceedings. This would enable domestic color picture tube companies, for example, to file and participate in Antidumping and Countervailing Duty cases on color televisions.

- It amends the definition of subsidy to make countervailable the provision of goods or services which are on terms inconsistent with commercial considerations, as well as loans, loan guarantees and equity infusions which are on preferential terms. This would permit the Commerce Department, for example, to countervail against the Canadian government's "stumpage" payments to Canada's softwood lumber industry if such payments were inconsistent with commercial considerations.

- It specifies the kinds of commitments to eliminate subsidies that foreign governments would need to make in order to qualify for (and continue to get) the injury test under Countervailing Duty law. This would require, for example, that Mexico and other advanced developing countries phase-down and eliminate export subsidies promptly; that the President review compliance on an annual basis; and that the injury test benefit be withdrawn in the event of non-compliance.

- It eliminates the Commerce Department's authority to suspend Countervailing Duty cases on the basis of foreign government export taxes. This would have precluded the Commerce Department, for example, from suspending past CVD cases on Brazilian steel in this manner.

- It waives preliminary ITC injury determinations in Antidumping and Countervailing Duty cases involving products for which there have been recent findings of injury. This would allow domestic companies, for example, to save the time and expense of a preliminary injury determination in "revolving door" cases involving multiple suppliers of the same product.

- It provides for a number of important procedural changes, including: (1) more rational procedures for the disclosure of confidential information under administrative protective order; (2) various limitations on the Commerce Department's authority to conduct "quick and dirty" 90-day reviews of Antidumping orders; and (3) elimination of the ITC role in determining whether "critical circumstances" exist to trigger the retroactive application of duties.

Title II - Improvements in Section 201 (the "Escape Clause")

This Title does the following:

- It eliminates the current role of the President and makes the USTR the "administering authority". This would help depoliticize Section 201 cases.

- It replaces the requirement that imports be the "substantial cause" of serious injury with the requirement that they merely be the "cause" of serious injury. Had this been law in 1980, it is probable that the Ford/UAW petition would have produced an affirmative injury vote.

- It makes relief more effective and certain by strengthening the "threat of injury" concept; precluding adjustment assistance as the sole form of relief; allowing for provisional relief measures in the early stages of investigations if import surges occur; requiring USTR to consult with foreign governments that have contributed to serious injury by targeting export markets or restricting imports of the product; allowing major parts and component producers to file and participate in proceedings; requiring USTR, if dumping or subsidization is uncovered, to consult with affected U.S. companies and workers about taking appropriate action under the Antidumping and Countervailing Duty laws; and permitting petitioners to reapply for relief in less than two years if good cause is shown.

- It establishes an optional alternative procedure designed to provide greater assurance that the relief provided is consistent with the requirements of enhanced competitiveness or adjustment to new methods of competition facing the industry. This involves the voluntary establishment of a tripartite advisory group to assess current problems and recommend a strategy to enhance competitiveness.

Title III - Improvements in Section 301 ("Enforcement of U.S. Rights")

This Title does the following:

- It eliminates the current role of the President and the interagency Section 301 Committee, and makes the USTR the "administering authority". In addition, it provides for strict investigatory and decision-making time lines; written questionnaires to foreign governments; verification of information submitted by foreign governments; and disclosure of confidential information under administrative protective order. These changes would help depoliticize Section 301 and make its procedures more like those in Antidumping and Countervailing Duty cases.

- It defines the term "targeting" and requires the USTR to take corrective action on behalf of domestic companies and workers injured by foreign industrial targeting.

Title IV - Negotiating Objectives

This Title does the following:

- It clarifies that all U.S. products and services, not just high technology products, should be accorded maximum access to foreign markets.

- It authorizes USTR to enter into negotiations aimed at strengthening GATT rules governing conduct by state-owned or controlled enterprises that engage in international trade. Such talks would seek to establish objective standards for determining when state-owned or controlled enterprises are operated on terms inconsistent with commercial considerations.

S. 1493

THE COMPREHENSIVE TRADE LAW REFORM ACT OF 1985

SECTION-BY-SECTION ANALYSIS

TITLE I - COUNTERVAILING AND ANTIDUMPING DUTY LAWS

SECTION 101 - LIMITATIONS ON ACCEPTANCES OF COUNTRY UNDER THE AGREEMENT

This section amends Section 701 of the Tariff Act of 1930 by requiring that countries "under the Agreement" must commit themselves under the General Agreement on Tariffs and Trade to eliminate export subsidies within one year; not to increase existing export subsidies; not to extend such subsidies to new merchandise or introduce new export subsidies; and to eliminate immediately export subsidies on merchandise which the ITC finds is already competitive in the U.S. market and would be competitive without such subsidization. Least developed countries, as defined in Section 124 of the Foreign Assistance Act of 1961, as amended, are allowed a transitional period of five years to phase out export subsidies, as opposed to higher income developing countries that must eliminate the subsidies promptly.

The Administering Authority would be required to review compliance with the commitments once a year. If noncompliance were found, the designation would be withdrawn. If the withdrawal occurred after the Commission had made a negative injury determination or after an order has been revoked, the negative determination of revocation would be voided.

SECTION 102 - ITC REVIEW OF CRITICAL CIRCUMSTANCES

This section revises the procedural aspects of antidumping and countervailing duty law in four ways:

(1) Instead of requiring a petitioner to allege critical circumstances, the ITA would be required to begin a critical circumstances investigation on the date that it initiates the dumping or subsidies investigation. It would publish a "notice of import surge" whenever it found evidence that imports have increased significantly in response to the filing of the petition.

(2) The ITC would be required to make an affirmative critical circumstances determination if the ITA has made an affirmative critical circumstances determination and if the ITC has made an affirmative material injury determination (not a threat only or retardation of establishment only determination).

(3) The ITA would direct Customs to suspend liquidation of entries under investigation entered 90 days before the anticipated date of the preliminary determination. If no critical circumstances determination is made, Customs would be ordered to liquidate all imports entered before the date of the preliminary determination.

(4) Countries that are not "countries under the Agreement" would be made subject to the critical circumstances provisions of the countervailing duty law.

SECTION 103 - PERSISTENT DUMPING AND SUBSIDIZATION

This section amends Sections 703 and 733 to waive the requirement of a preliminary determination by the Commission in any instance where the Administering Authority determines that, during the year preceding the filing of a petition, the Commission had made a preliminary or final affirmative determination with respect to the same product. This section therefore dispenses with the requirement of a preliminary determination in those instances where successive petitions are filed to deal with imports of the same product from many different countries. In addition, it provides for the waiver of preliminary injury determinations in such instances, without regard to whether the preceding injury determination was made under antidumping or countervailing duty law with respect to investigations of that product.

SECTION 104 - SUSPENSION OF INVESTIGATIONS

This section amends Section 704 (b) to prevent the Commerce Department from suspending a CVD investigation based on a promise by a foreign government to apply an export tax equal to the determined net subsidy (otherwise known as an "offsetting" export tax), thus eliminating the export tax as a basis for suspending a CVD investigation.

SECTION 105 - LIMITED APPLICATION OF 90-DAY REVIEW AUTHORITY

This section amends Section 736(c) by adding three new critera for the institution of expedited reviews of AD orders, and allows for written comments by interested parties before the decision is made to conduct such a review. The additional criteria include: (1) normal AD time lines; (2) evidence of a significant anticipated margin differential; and (3) representative sales as the basis for review.

SECTION 106 - COUNTERVAILABLE SUBSIDY DEFINITION

This section amends the definition of subsidy to make countervailable the provision of goods or services which are on terms inconsistent with commercial considerations (as well as on preferential terms). In addition, it makes countervailable loans, loan guarantees and equity infusions which are on preferential terms (as well as on terms inconsistent with commercial considerations). At present, only the provision of goods or services on preferential terms and/or loans, loan guarantees and equity infusions on terms inconsistent with commercial considerations are countervailable.

SECTION 107 - COMPONENT PART PRODUCERS TREATED AS INTERESTED PARTIES

This section defines "interested party" to permit participation in AD & CVD proceedings by those associated with the production of major parts and components intended to be incorporated into the imported article.

SECTION 108 - DIVERSIONARY DUMPING

This section does the following:

(1) It establishes a new Section 771(18) definition of "Diversionary Dumping" that permits a less than fair value dumping analysis to be applied to an input which is the subject of an outstanding antidumping order against the manufacturer or producer of the material or component, as well as to an input which is the subject of a suspension agreement or other arrangement affecting the material or component.

(2) It amends Section 773(a) to include an adjustment amount for diversionary dumping in determining foreign market value.

(3) It amends Section 773(b) to include an adjustment amount for diversionary dumping in determining sales at less than cost of production.

(4) It amends Section 773(e) to include an adjustment amount for diversionary dumping in determining the constructed value of components as well as materials.

SECTION 109 - UPSTREAM SUBSIDIES

This section does the following:

(1) It amends Section 771A(a) to enlarge the third-country application of the upstream subsidy provisions to subsidies paid or bestowed under the authority of a customs union or its members.

(2) It establishes a new Section 771A(b)(3) "special diversion" rule creating a presumption of competitive benefit for an input product where there is a prior subsidy finding or the input product is subject to an arrangement which results in increases in imports of the investigated product.

Section 110 - DISCLOSURE OF CONFIDENTIAL INFORMATION

This section amends Section 777 to make clear that continuing disclosure is to take place pursuant to one application that describes, in general terms, the type of information sought. The initial application may be filed before any information is submitted by any party and may list and request all of the types of information that may be submitted in the case. This application would operate as an ongoing request for release. In addition, this section specifies strict time lines for the release of information under APO, to ensure that current procedures are improved. With regard to those parties that oppose release, such parties would be required to state at the time the information is submitted both why they oppose release and whether they want to withdraw the information should the Commerce Department decide release is justified. Finally, this section requires disclosure of confidential information submitted under a properly filed APO, unless the submitter proves disclosure will cause substantial harm to its business operations, and that such harm outweighs the requester's need for the information.

TITLE II - RELIEF FROM INJURY CAUSED BY IMPORT COMPETITION

SECTION 201 -- INVESTIGATIONS UNDER SECTION 201 OF TRADE ACT OF 1974

This section amends Chapter 1, Title II of the Trade Act of 1974, dealing with authority to grant temporary import relief to injured industries following investigations by the International Trade Commission. In the past, the ultimate decision to grant import relief has rested with the President. This section transfers that authority to the Administering Authority.

This section includes enhancement of an industry's competitiveness as a purpose for which import relief can be sought.

Standing is given to an industry that produces materials, parts, components or subassemblies irrevocably destined for incorporation in an article like or directly competitive with an imported article.

This section replaces the requirement that imports be the "substantial cause" of injury with the requirement that they be merely "the cause of injury." The term "cause" is defined as a cause which is important, even though another cause or other causes, such as a general economic recession, may be of equal or greater importance.

This section also lists additional factors for the International Trade Commission (ITC) to consider in making a determination of threat of injury. These include (1) a decline in market share; (2) higher and growing domestic inventories; (3) a downward trend in production, profit, wages or employment; (4) foreign industrial targeting; and (5) the extent to which diversion of exports to the U.S. market occurs because other markets are closed. The section also provides that imports by domestic producers shall not be considered a factor indicating the absence of serious injury, or threat thereof. If injury is found to exist, the ITC must recommend relief, even if the relief will only assist in remedying the injury. The ITC may also recommend adjustment assistance in addition to increased duties or import restrictions.

SECTION 202 - PROVISIONAL RELIEF UPON FINDING OF CRITICAL CIRCUMSTANCES

This section adds a new subsection to Section 201 of the Trade Act of 1974, permitting the Administering Authority to impose provisional measures should it find that critical circumstances exist. Critical circumstances are defined as instances where a delay in inhibiting a significant increase in imports which occurred over a short period of time would cause damage difficult to repair. Provisional measures may consist of duty imposition, tariff-rate quotas, quantitative restrictions, orderly marketing agreements or any combination thereof. These measures would remain in force until the President revokes them, the ITC makes a negative determination, or 60 days after the ITC makes an affirmative determination.

SECTION 203 - CONSULTATIONS WITH FOREIGN GOVERNMENTS

This section amends Section 201 of the Trade Act of 1974 to provide that when the ITC makes an affirmative recommendation to the Administering Authority, it shall determine whether the foreign government concerned engaged in actions to expand export markets or to restrict imports of the article, and whether diversion of exports to the United States has occurred because other markets are closed. If the ITC determines that either of these conditions has occurred, and the Administering Authority decides to impose import relief, the Administering Authority must consult and negotiate with other producing and consuming countries to seek to establish a multilateral framework for the maintenance and development of fair, equitable and non-disruptive patterns of trade.

SECTION 204 - INDUSTRY ASSESSMENT AND COMPETITIVENESS STRATEGY

This section adds a new Section 204, entitled "Industry Assessment and Competitiveness Strategy." The section accords firms and workers representing a significant portion of the industry the right to request the establishment of an ad-hoc industry advisory group to prepare an assessment of current problems and a strategy to enhance competitiveness for the industry. The assessment and strategy is to set forth objectives and specific steps which workers and firms could usefully undertake to improve the industry's ability to compete or to assist the industry to adjust to new methods of competition. The advisory group is to include in its report a determination of the ability of producers in the industry to generate adequate capital to finance the modernization of plant and equipment, or to otherwise enhance competitiveness, including an estimate of the overall capital requirements of the industry. Copies of the assessment and strategy are to be submitted to the ITC, the Administering Authority, and the Secretaries of Commerce and Labor within 120 days after the ITC began the investigation. The membership of the group is to include appointees of the Administering Authority who are representative of workers and the industry, and employees of the Departments of Commerce and Labor. Staff is to be provided by the Secretaries of Commerce and Labor.

After the assessment and strategy is completed, the Administering Authority will seek to obtain, on a confidential basis, information from individual members of the advisory group concerning how they intend to act upon the recommended objectives and actions in the assessment and strategy, or other actions they intend to take to enhance competitiveness. Such information will be shared, on a confidential basis, with the ITC and the Secretaries of Labor and Commerce.

Failure to prepare an assessment and strategy for the industry may not be a factor considered by the ITC in making either its injury determination, or its relief recommendation, nor may it be a factor in the relief decision of the Administering Authority. The ITC is, however, required to take account of such assessment and strategy in making its recommendation regarding the appropriate relief.

The ITC is also to consider, as a factor in evaluating threat of substantial injury, the inability of producers in the industry to generate adequate capital to finance plant and equipment modernization or enhance competitiveness, as provided in the assessment and strategy.

This section requires the Administering Authority, in determining what, if any, relief to provide an injured industry, to evaluate the assessment and strategy and take account of the probable effectiveness of import relief as a means to improve competitive abilities. The Secretaries of Labor and Commerce are also required to take account of the assessment and strategy in developing their advice.

This section also provides that when import relief is granted and an assessment and strategy for the industry has been prepared, the Administering Authority is entitled to rely upon the actions outlined in the assessment and strategy, and individual confidential submissions, as one basis for granting relief. The Administering Authority is also to establish a review committee, comprised of itself and the Secretaries of Commerce and Labor, to monitor actions taken to improve the competitive position of the industry, including actions described in the confidential submissions. If, after consultation with the advisory group, the review committee considers that recommended actions and objectives in the assessment and strategy or intended actions described in confidential submissions are not being implemented, or are being unsatisfactorily implemented, and that the failure to implement them is not justified by changed circumstances and has adversely affected the overall implementation of the objectives in the assessment and strategy, then it must so notify the Administering Authority. The Administering Authority will then ask the Commission to report under Section 203(i)(2) on the effects of removing relief. After receiving the Commission report, the Administering Authority will immediately consider whether import relief to the industry should be terminated or modified.

SECTION 205 - IMPORT RELIEF

This section provides that if the Administering Authority determines that import relief is appropriate, the Administering Authority shall consult with petitioners and industry representatives as to the advisability of taking action under the countervailing duty provisions of U.S. trade laws or under Title III of the Trade Act of 1974, where there is reasonable cause to believe that such actions would be appropriate.

TITLE III - RELIEF FROM INJURIOUS INDUSTRIAL TARGETING AND UNFAIR TRADE PRACTICES

SECTIONS 301 - ENFORCEMENT OF UNITED STATES RIGHTS UNDER TRADE AGREEMENTS AND RESPONSE TO INJURIOUS INDUSTRIAL TARGETING AND OTHER FOREIGN TRADE PRACTICES

This section transfers all Section 301 authority from the President to the Administering Authority, and authorizes the Administering Authority to act in response to injurious industrial targeting. This practice is defined as any combination of coordinated government actions, whether carried out severally or jointly which: (a) are bestowed on a specific enterprise industry or group thereof, (b) assist such enterprise, industry or group to become more competitive in the export of any class or kind of merchandise, and (c) cause, or threaten to cause, material injury. In addition, this section requires the Administering Authority to consult with representatives from industry and labor prior to reaching any determination; authorizes various actions (including duties, restrictions and negotiated agreements) to restore or improve the international competitive position of the affected domestic industry; and requires that confidential information submitted during an investigation be available for disclosure under administrative protective order.

SECTION 302 - INVESTIGATIONS UNDER TITLE III OF THE TRADE ACT OF 1974

This section requires written questionnaires and verification of all information submitted by foreign governments and corporations; specifies strict time lines in regard to preliminary and final determinations; and requires submission of a written statement to the Congress if the final determination was affirmative and the Administering Authority declines to take any action.

SECTION 303 - MANDATORY ACTION IN CASES OF INJURIOUS INDUSTRIAL TARGETING

This section establishes a separate track for investigations of injurious industrial targeting and, upon an affirmative ITC material injury finding and an affirmative determination by the Administering Authority, requires that the Administering Authority take at least one of a number of described actions to offset the material injury or the threat of material injury from such targeting. In addition, when the Administering Authority determines preliminarily that targeting has occurred, it requires establishment of an advisory committee (composed of representatives of affected domestic firms and workers as well as appropriate federal officials) to develop proposals to improve the competitive position of the industry affected by such targeting.

TITLE IV - NEGOTIATING OBJECTIVES

SECTION 401 - FOREIGN MARKET ACCESS FOR ALL PRODUCTS;

This section amends Section 104 of the Trade Act of 1974 to clarify that the United States objective of securing maximum access to international markets extends to all products, not just high-technology products. In addition, it clarifies, as a principal U.S. negotiating objective, the elimination of those acts, policies, or practices identified in Section 181 which deny national treatment to U.S. industries.

STATED-OWNED OR CONTROLLED ENTERPRISES

This section amends Sections 102 and 121 of the Trade Act of 1974 to require that the United States undertake efforts to secure an international agreement on rules and procedures to evaluate and respond to the maintenance of state-owned or controlled enterprises. This section also specifies the desirable terms of such an agreement and urges the United States to negotiate on the expansion and revision of Article XVII of the GATT (relating to state-controlled enterprises).

The Chairman. Mr. Calvert, let me ask you a question involving natural resources, but it is timber, which I know better, rather than natural gas.

Western United States, the northwestern United States, and western Canada have similar histories. The areas were unsettled, the Governments moved West, the Governments became the owners of immense tracts of timber, both in British Columbia and in Oregon and in Washington.

The Canadian Government chooses to give away their timber at a relatively low price. They don't sell it on a bid basis; although I don't think they are losing money on it, they didn't have any money in it. They just absorbed it.

The United States chooses to sell its public timber by bid, to the highest bidder, which makes the American timber significantly higher priced than the Canadian timber. And it makes their timber, therefore, more competitive. It is the same species of timber, but it makes it more competitive in our markets than our timber because they have a lower natural resource price.

Are you saying that Canada must play by our rules? They have got to sell their timber to the highest bidder, or we will call it "an unfair trade practice," or they can't sell in our market?

I emphasize that they are not giving any preference to their markets over ours; they sell it to their same producers no matter where they are selling it. It is just the way they happen to dispose of their timber in Canada.

Mr. Calvert. No, sir; I don't think so, if I understand your question correctly. I assume that if a U.S. private company wanted to go into Canada and form the proper Canadian company, that it would have access to the same timber rights as Canadian companies.

The Chairman. There are some limitations on investment. By and large, a number of American companies operate in British Columbia and buy the timber on the same basis.

Mr. Calvert. All right, sir.

So, our main thrust relative to the imports of nitrogen relate to those countries such as Russia, Romania, some other Eastern bloc countries, and Mexico, where our U.S. private companies do not have access on the same basis as the state-owned enterprises.

The Chairman. So you would have no objection if U.S. companies could go to Mexico and set up operation, and buy very low-priced natural gas, even though America had competitively priced gas you would have no objection in that case? So long as the American companies had access to set up an overseas or a Mexican operation?

Mr. Calvert. If we have access on the same basis, then that is our choice.

The Chairman. All right.

Now, Mr. Conner, let me ask you a question. First I will go back to Mr. Calvert.

That of course lends itself to American companies going overseas and producing overseas, or in Mexico's case producing in Mexico?

Mr. Calvert. Yes. But that clearly is our free choice. Today we have no choice.

The CHAIRMAN. Do our foreign competitors have to observe all of the practices we have? Do they have to have the same environmental laws, the same occupational health and safety laws, the same minimum wage laws, so that when they compete with us they are competing on the same playing field? What are the things that are fair and unfair in your estimation?

Mr. CONNER. Well, with regard to the specific question that you asked, there is one standard that has cost our textile industry a great deal of money, the compliance with OSHA's cotton-dust standard. I am not here to debate whether it is a good standard or a bad standard; I think it certainly is a commendable effort to try to take care of a problem that is perceived.

I discussed this very thing and asked about what was done by a Taiwanese mill, and the answer was, "We cannot be concerned with health problems in our mills; we are a developing nation."

The CHAIRMAN. Well, I understand that. I know they don't have the same OSHA laws. They don't have the same air and water quality laws. They don't have anything the same. Must they have the same or something closely equivalent to it, or we won't allow their products in this country? In other words, is our standard going to be the world's standard?

Mr. CONNER. Well, I think each country has to make these decisions on their own; but certainly I think it has to be recognized that, if we are going to live by a different standard, that it is a different additive of cost in our manufacturing.

The CHAIRMAN. Let me ask you a further one: If we choose, then, to live by a much higher wage standard—and the industries I will cite to you particularly were the automobile industry and the steel industry, where for years they had no foreign competition, and they were all unionized, and it did not matter what wage they paid so long as they all paid the same wage.

Are you saying, given this situation, we should still say, "Unless the Japanese automobile companies are going to pay their workers $23 to $24 an hour, they cannot sell cars in this market"?

Mr. CONNER. Well, I don't like to compare industries. Certainly, I don't think in our case, in the textile industry, if you look at it historically, that we have quite the same comparison as the automobile industry.

At the same time, I think what you are saying, sir, is are we willing to go to the American people and ask them to work for 10 cents an hour, as they do in Bangladesh? I think there is a point that is both politically untenable and also is not practical. I don't think you are going to find American people who are willing to say, "Fine, if we have to compete and wage rates are the difference with what it is in Bangladesh or some of these other countries"—I don't think you are going to find the American people willing to make that sacrifice.

The CHAIRMAN. Well, then there is the conclusion that, where we have wage differentials, health differentials, safety differentials, pollution differentials, basically our policy will be, "We will put up the barriers, be they tariffs or quotas or whatever, and we will really only manufacture for our market and sell in our market. we won't buy anything overseas except for raw materials in short supply, and we really won't try to sell anything overseas. We will just be a self-contained unit of 240 million people."

Mr. **Conner**. Well, no, sir. I wouldn't advocate that. In fact, in our own case, we have tried very much to export. As a matter of fact, it is our belief that the American yarn-producing industry is as efficient if not more so than any in the world. We have some products in our area where the labor content is only 5 to 7 percent of the manufacturing cost.

Now, if you look at Taiwan or Korea, where certainly power costs are higher and other costs are higher, for example, petrochemicals for fiber production, how can they sell in competition with us worldwide with such a low labor cost not really being a factor on either side at as much as 15 to 20 percent under our manufacturing cost? It doesn't make sense. Obviously there are some sorts of subsidies and government assists.

Generally the way these things take effect in our industry is that the foreign government provides entry-level assistance to get the companies starting and up and running.

The **Chairman**. Senator Baucus.

Senator **Baucus**. Thank you, Mr. Chairman.

Mr. Calvert, as I understand your response to Chairman Packwood's question to you, you said that so long as a country makes its natural resource subsidy available both to domestic companies as well as to foreign companies in that country, that that is okay because it is up to an individual firm to just shop around and to, wherever it wants to, buy say a product. Is that right? Is that what you said?

Mr. **Calvert**. I am sorry?

Senator **Baucus**. Essentially you say, as I understand your point, that you feel that it is okay for a U.S. company say to go to some other country, and it is OK for that other country to have a natural resource subsidy, so long as that subsidy is—to use a term of art around here—"generally available" to both domestic companies as well as, in this case, the United States—a foreign country in that country.

Mr. **Calvert**. Let's take the case of Romania and the Soviet Union. What we have done at this point in time is to give our market to them, in the case of fertilizer, taking it away from our U.S. companies. We have opened the door.

But we as a company do not have any access to that low-priced natural resource in country or for export.

Senator **Baucus**. Now, turning again to Canada, the Canadian Government does provide a natural resource subsidy to Canadian companies who purchase Canadian timber. The Canadian stumpage rates are very, very low. The problem is that United States companies, although they can set up shop and set up mills and buy that timber at the low stumpage rates in Canada, they cannot export the logs to United States mills. That is, Canada has a prohibition; it does not allow the effect of that lower stumpage rate natural resource subsidy to apply to American firms who go to Canada to try to buy their logs. Do you think that would be unfair.

Mr. **Calvert**. You are getting me into an area that I know absolutely nothing about.

But in the case of fertilizer people going to Canada, they do not have access to natural gas for their fertilizer production in Canada.

Senator BAUCUS. But American companies cannot buy Canadian logs and ship them to United States mills. They cannot do that.

Mr. CALVERT. Well, that doesn't sound right to me.

Senator BAUCUS. Mr. Harrington, what about that?

Mr. HARRINGTON. Senator, the question seems to focus on a key aspect of the problem here. We seem to be talking about access as opposed to any subsidy practice. We do not believe there is a subsidy practice; we think there is a comparative advantage that Mexico has.

Senator BAUCUS. But I am talking about Canada. I don't know as much about Mexico. But for the Canadian problem you don't think that is a subsidy? Canadian stumpage?

Mr. HARRINGTON. I can only say about Canada, because I am not that well-versed on the issue, that I understand there are a lot of sensitivities there, and it is a problem that needs to be worked on. But really, we have been focusing from Cargill's perspective on the petrochemical side of the natural resource subsidy question.

Senator BAUCUS. Let me ask, aren't natural resource subsidies, as a matter of principle, wrong? The United States has signed a subsidies code, Canada has signed a subsidies code, I guess Mexico has signed a subsidies code, basically providing that subsidies are as a matter of principle something that a country should not practice. So, why in the world, as a matter of principle, should a country provide a natural resource subsidy?

We all worship at the alter of free competition around here; so, why don't we be consistent? Why don't we want to have it both ways?

Mr. HARRINGTON. If I may respond, I think Professor Jackson hit on quite a bit of the answer to that question, and it comes down to the problem of how do you define a subsidy? Is government-provide schooling a subsidy for greater productivity down the road? The list goes on and on.

We have a number of practices in the United States that could be affected by mirror legislation if natural resource legislation were enacted overseas—hydropower, for example, is provided at low rates. And certainly in agriculture there are a number of subsidy practices that are used by our government.

So, it is as much a problem of definition as anything.

Senator BAUCUS. Thank you.

The CHAIRMAN. Senator Long.

Senator LONG. Mr. Chairman, I have a number of questions to ask, and it would run over my five minutes. I would be happy to wait for the others, to see if they ask those questions, and then ask mine last.

The CHAIRMAN. All right.

Senator Boren.

Senator BOREN. Thank you very much, Senator Long.

Mr. Chairman, first I want to welcome Bill Calvert from Agrico to our committee. Their headquarters are in Tulsa, and he is certainly one of our most able and knowledgeable business leaders.

You talked about the natural resource policy in other countries, that we have in essence or at least are moving toward a deregulated atmosphere here, and Canada is also moving toward a deregulated atmosphere, in the pricing of our natural gas, for example, and our other energy components.

In what ways do other governments manipulate the pricing of their products to create an unfair advantage?

Mr. CALVERT. Well, perhaps a good example would be the import of urea over the past 6 or 8 months. During that period of time, through the decontrol of natural gas, the actual market price of natural gas has gone from roughly $3 per million Btu in the United States down to $2.50 to $2.75. So that means the cost of the natural gas going into our U.S. plants has been reduced.

Senator BOREN. Right.

Mr. CALVERT. So, you would suspect that in the process perhaps we ought to make a bigger profit; but that hasn't been the case. As those costs have come down, the price of the imported material coming into the United States has come right on down. We are from a profit standpoint, probably going to make less money this year than we have before.

Senator BOREN. How have the governments of these other countries done this? Have they just made it directly? Since they control price—they don't have a free market price; the government sets the price for a particular industry—have they just simply lowered the price, let's say, to those producers that are competing with you in their own country?

Mr. CALVERT. That is correct.

Senator BOREN. Has that been true in Mexico?

Mr. CALVERT. Yes. Mexican ammonia coming in here has been produced using this advantage, as has urea from Romania and the Eastern Bloc countries.

Senator BOREN. And as you said, you would have no access, if you decided to go put up a plant in either one of those countries, to natural gas at the same price?

Mr. CALVERT. That is right.

I think we ought to distinguish. Mexico, a few years back, was exporting natural gas to the United States at a very high price; at the same time they were supplying gas to their own industry at a very low price.

Senator BOREN. At a very small fraction of what they were charging us in terms of the exports.

Mr. CALVERT. That is correct.

Senator BOREN. Mr. Harrington, I am very concerned about agricultural exports, and I have been very reluctant to support certain bills, including one that was on the floor of Senate just last week, for fear of the impact it would have on agricultural exports. But on the other hand, don't we have an obligation to protect our own industries against unfair practices? I would hate to see us 100-percent dependent for fertilizer, speaking as one concerned about agriculture, on overseas sources.

Do you defend these kinds of manipulations of pricing by governments of other countries? Do we have no obligation at all toward our own domestic suppliers to stop this kind of practice in your opinion?

Mr. HARRINGTON. Well, first of all, I mentioned before that we have a parochial interest in this legislation. Cargill imports nitrogen fertilizer in various forms. And we also have a domestic production in a small way in the Central States.

Nevertheless, I think we are talking mostly here about a cost advantage that the government has in that country. Let's take Mexico as an example.

Mexico is under a huge debt burden. It is trying to do everything it can to maximize its exports and the value of the exports—first, by selling the resource for whatever the world market will bear, and second, by adding value to that resource within its country and exporting that product to keep its own people employed. It becomes a very difficult thing when we start trying to dictate internal policies like that within an integrated corporation, for example; you have companies that will, if you want to call it "manipulate" the price of their exchanges of goods in the course of production. But we can't get in there and dictate to them how they should operate.

Senator BOREN. Well, with all due respect, we do have access to our markets through which we could bargain, and I don't see how in the world we can close our eyes. I think it becomes a little difficult here when we talk about fairness across the board in the economy, and I am very concerned about fairness with markets open for agricultural exports; but I have to, in all honesty, disagree with you. I don't see how in the world we can close our eyes to unfair manipulation of inputs and not call those unfair trade practices. They are no different than any kind of a direct subsidy or anything else. That is exactly what they are. They are manipulating and gaining access to our markets. I don't think we should allow it.

I have one last very brief question, Mr. Calvert. How many other nations have no tariffs on fertilizer imports, other than the United States?

Mr. CALVERT. The EEC has tariffs on exports from the United States to the European Common Market. We have a list of them that we would be glad to make available to you.

Senator BOREN. Is Hong Kong about the only one that does not have?

Mr. CALVERT. I'm sorry?

Senator BOREN. Is Hong Kong about the only area that does not have a tariff on this?

Mr. CALVERT. Well, Hong Kong does not use enough fertilizer to worry about, so I haven't worried about it.

Senator BOREN. Doesn't nearly every other country in the world have a tariff or a duty or a restriction of some kind?

Mr. CALVERT. That is correct: either a tariff or a licensing procedure, or some other sort of restriction. Latin American countries are noted for this kind of activity.

Senator BOREN. Would it be fair to say we are virtually the only major user in the world which doesn't have some kind of procedure that impedes the free flow of imports of those products, where you can have manipulation of inputs of imports?

Mr. CALVERT. Yes, sir, that is correct.

The CHAIRMAN. Mr. Conner, very quickly, on page 2 of your statement you refer to industries that are being clobbered by international trade, systematic decimation of America's industrial base.

Has America's industrial production gone up or down over the last 10 years?

Mr. CONNER. Well, I can only speak for the specific industry, in more specific terms, that I work with. And certainly, if you look back over the last 10 or 15 years—and it can be measured in a number of ways—yes, our level has gone down.

In terms of all manufacturing it depends on what you include. I couldn't give you an answer.

The CHAIRMAN. It has actually gone up. If you take the same industries—the same ones that were here 10 years ago, 20 years ago, 30 years ago—it has gone down in some industries and up in others. But in terms of total industrial production, it has gone up.

Mr. CONNER. Well, I think you would have to look beyond that, though, in terms of has it gone up in terms of consumption? Has American production kept up with increases in consumption? Or are we progressively conceding a larger share of the market to imports, with a lesser share of the total market going to domestic production?

The CHAIRMAN. Oh, there is no question that more manufactured goods are coming in. My question is: Are we decimating our production facilities? Are we deindustrializing America if indeed our production continues to go up?

Mr. CONNER. Well, here again, sir, I don't think you can expect any business or any industry to maintain a viability unless it has some potential for growth.

The CHAIRMAN. It is growing.

Mr. CONNER. Well, it is growing in relation to the market. Though, I think the important consideration's we are increasingly having a smaller and smaller share of the production produced here and a larger share coming in from overseas. In some industries this has caused some difficulties in terms of both its infrastructure, its ability to grow, its ability to maintain a viable corporate plan of development, and this sort of thing.

I think you have to look at it, really, more in terms of the market and what is really happening to our structure. I mean, there are many, many products that were produced in this country 10 or 15 years ago where we had the bulk of the market, for example many electronic products such as television. And now they are not even made here.

The CHAIRMAN. Maybe I will ask the question this way: Should American industrial producers be guaranteed a certain percentage of the American market?

Mr. CONNER. Well, I think there, again, you get into the questions of defense and so forth.

The CHAIRMAN. No; I understand that. Forget the defense aspects.

Mr. CONNER. If you are asking should you say that 80 percent of a particular product always should be produced in America, no, sir, I wouldn't say that is necessarily possible. I do think there is a point at which, for the long-term good of our economy, yes, we need to maintain a certain part of industries, or a certain part of an industry.

You could use the case earlier that was cited about the tanks: Could Chrysler exist if it only made tanks? I rather doubt it.

The CHAIRMAN. I will shift very quickly to another question. You indicate that section 201 is becoming too politicized, although in three out of the five cases that they have decided over the last years the President has gone along with the International Trade Commission. But would you be willing to live with the 201 procedure that took the President and the administration out of it totally and said, 'The International Trade Commission decision shall be final and not appealable'?

Mr. CONNER. I think so.

The CHAIRMAN. You would?

Mr. CONNER. Yes, sir.

The CHAIRMAN. With the President appointing the board members?

Mr. CONNER. I thought you said the International Trade Commission's decision.

The CHAIRMAN. I did. But I am saying the President nominates the members of the International Trade Commission.

Would you be satisfied to live with the decision of the International Trade Commission, and no appeal, no matter what the decision?

Mr. CONNER. Well, I believe the Congress also has some oversight on the appointments to the International Trade Commission.

The CHAIRMAN. We advise and consent, like we do to all others, but very, very, very seldom do we not approve a Presidential appointment.

Mr. CONNER. Which does provide a check and balance.

The CHAIRMAN. But you would live with that?

Mr. CONNER. Yes.

The CHAIRMAN. All right.

Senator Baucus, any other questions?

Senator BAUCUS. No questions, Mr. Chairman.

The CHAIRMAN. Senator Long.

Senator LONG. Mr. Conner, I once discussed with an executive of one of the major pipeline companies his experience in negotiating with the Soviet Union about the proposal to buy natural gas and bring it in from the Soviet Union. Now, that was back in the days when we talked about moving gas in ships; I am sure you are familiar with that, or, if not, Mr. Calvert is familiar with the technique of moving gas around on ships. I think you would move it in liquid form.

He told me that in negotiation with the Soviets, he became concerned that, by their estimates, the Soviets were not going to be receiving anything for that gas at the well heads, that it would all be consumed in the cost of the transportation.

So, he pointed that out to them and said, "I think you ought to understand this, that according to our estimates, having done this through our computers, it looks to us very much as though, if this contract is concluded, and apparently you are willing to sign it with us, it will mean that you are receiving zero at the well head, that the cost of the transportation will eat up the entire cost of this contract. And I hope you understand that is the case, because that is how it looks to us."

He said that those who were negotiating for the other side smiled and said, "Well, that it because you do not understand how we keep our books."

Mr. CALVERT. I can appreciate that.

Senator LONG. Now, what does that mean to you?

Mr. CALVERT. That means they don't keep any books. As I said in my statement, if you take the price of urea today that is sold by the Soviet Union, and back out the transportation and manufacturing costs back to the wellhead, you would get a minus figure for the natural gas price. The answer is that they don't keep books like we do.

What they are really trying to do, Senator, is generate hard currency. And as long as they can sell that product and bring home some dollars, they are satisfied—as opposed to leaving gas in the ground.

Senator LONG. Then I would take it from that exchange that if this fellow had pursued it further and asked, "Why would you want to do that?" They would say, "Well, that is our business. If we make the deal, it is none of your business what we would do with the money." And I would assume that they wanted those dollars for reasons that they would rather not go into detail in discussing. Does that make sense to you?

Mr. CALVERT. Yes, sir, it does.

Senator LONG. So, in trading with the Soviet Union or some of the other Eastern bloc countries, you have to keep in mind that they are not thinking in the same terms as we are, such that the producer has to show a profit so he can afford to continue to drill wells. It is entirely a different matter for them. One system is trading with the other, and the considerations on which they trade are completely foreign to us.

Mr. CALVERT. Yes, sir, I agree with you.

Senator LONG. And there is probably not much a Harvard professor can teach us about how they keep their books, is there?

Mr. CALVERT. That is correct.

Senator LONG. Now let me ask you this: Has the congressional interest in the natural resources problem resulted in any change in the Mexican practices about natural gas?

Mr. CALVERT. I'm sorry, I didn't understand you.

Senator LONG. We in Congress have been trying to do something about Mexican natural gas practices. We have managed to get as far as the conference with the proposal to try to do something about the use of natural gas to subsidize chemical exports, and also to give Mexican producers the advantage in manufacturing and selling cement. I just wondered if you would know if the congressional interest in this natural resources problem resulted in any change in the Mexican practices.

Mr. CALVERT. No, sir, not in our industry. I don't see any evidence of that whatsoever.

Senator LONG. You mentioned in your testimony that the GATT provisions on state trading, GATT article XVII. Do natural resources subsidies violate the GATT?

Mr. CALVERT. According to my attorney who is an expert on it, I think the answer would be yes.

Senator LONG. In September, the Court of International Trade reversed the Commerce Department decision that a Mexican petroleum subsidy was not actionable in the carbon and black industry. Does that decision eliminate the need for this natural resources legislation?

Mr. CALVERT. No, sir, Senator. We have been fighting this problem for over 6 years, the group of us—the Mexican problem, the Russian problem—and we have gotten nowhere using existing laws.

Senator LONG. Are American facilities for producing ammonia less efficient than the competing Mexican facilities?

Mr. CALVERT. Absolutely not. We are more efficient than they are in terms of building the plants and operating the plants. The problem is the input price of the natural gas.

Senator LONG. In other words, if you assume that we are paying the same price that they are paying for natural gas, could we prevail in our market on a free competitive basis?

Mr. CALVERT. Absolutely. We could prevail in our market as well as in the world market.

Senator LONG. So the problem is purely the matter of the subsidy? In other words, it is a matter of putting the natural gas into the product at a price far below the price that we are paying?

Mr. CALVERT. That is absolutely correct.

Senator LONG. Now, sometime ago we negotiated with the Mexicans, and I really think it would have been a good deal for both countries. In fact, during the energy crisis this nation sought to make a contract with Mexico to buy a lot of Mexican natural gas to be delivered into the United States to be used for whatever purpose we might need here in this country. Are you familiar with the fact that such a negotiation happened?

Mr. CALVERT. Yes, sir.

Senator LONG. And the agreement did not happen. The Mexicans were not willing to sell at the same price that the Department of Energy was willing to recommend. It always seemed to me that Mr. Schlessinger was making a bad mistake when he wasn't able to make the contract, because I thought it was very advantageous that we get a commitment for that Mexican natural gas to supplement our energy resources in the United States.

Right now, of course, we have a big surplus of gas, partly because the price of oil went up and partly because we deregulated the price here in the United States.

Mr. CALVERT. That is correct.

Senator LONG. But at some future point we will be needing more natural gas, and it seems to me it is to our advantage to buy it.

Now, in my part of the world, even though we produce a lot of it, we are a surface producer. We have to share it with the rest of the United States under contracts made many years ago. We wanted to buy whatever would be earmarked as our share of the Mexican natural gas at the price the Mexicans were asking. Now we find that they are putting their natural gas into ammonia and really pricing it backward. They look at their costs, and first they put in the cost of selling and delivering in the United States. Then they put the cost of transportation, then they will come back to Mexico and add the cost of the labor, then they will add in the cost—at least I'm told it is this way—of interest on the money, and the depreciation, and so forth. The last item they get to is the natural gas. And they price it as they need to serve their purpose.

Now, if they are not going to sell gas outside Mexico, they have got very limited market inside Mexico to sell all that natural gas to, have they not?

Mr. **Calvert**. Correct.

Senator **Long**. So they are in position to sell it very, very cheaply, even though we are willing to pay them. Now, of course, it would have to be delivered by pipeline; but my understanding is, what we Americans mainly want, if they want to do business with us, is to buy natural gas, not to go down there into Mexico and make it into ammonia, but we would like to make it up here.

Mr. **Calvert**. Yes, that would be more efficient.

Senator **Long**. It would seem to me that could be used just as any other substance could be used, to whatever extent needed to put you out of business.

Mr. **Calvert**. Yes, that's correct.

Senator **Long**. There are a couple of other things I wanted to ask about here.

You mentioned the provision in trade law that sets out one of the criteria for countries like Mexico to receive a preference for duty-free entry of their exports under our Generalized System of Preferences for Developing Countries. What is the significance of this provision to you as a businessman?

Mr. **Calvert**. Senator, it is my understanding that this particular provision has been in our law for at least 10 years. This makes it very clear, as a matter of principle under U.S. trade law, that any country which discriminate and restricts access to a basic commodity resource or resources, is doing something unfair and inequitable.

Senator, it seems to me that one of the basic problems that we are concerned with an that we are confronting has already been determined to be an unfair practice in U.S. law, and that it has been viewed as such for over 10 years.

One of the problems I see with this particular law is that it specifically does not apply to Communist countries or OPEC countries, where most of our problems are coming from.

In addition, almost none of these countries are members of GATT, and in one way or another, most of our trade laws either do not apply to these countries or are ineffective, because the President will not exercise discretionary authority provided by the Congress under section 406, 301, or 201.

As you are well aware, our countervailing duty laws are also inadequate, which is why we support Senate bill 1292—which you cosponsored with Senator Baucus—to address natural resource subsidies.

I am no trade expert and do not fully understand all the reasons why our subsidy laws don't apply to Communist countries, and I don't really understand why we have to use some other countries to determine whether a Communist country is dumping in the United States; but I do understand that this law is essentially like shooting craps: it depends on the luck of the roll.

In a recent case on potash fertilizer, the preliminary decision was based on production costs in West Germany, and resulted in duties of more than 100 percent.

Then the surrogate country was switched to Canada, resulting in no duties at all.

I am generally familiar with the subsidies case on Mexican ammonia, which is the reason we have supported Senate bill 1292 to amend the countervailing duty laws that deal with this problem. There doesn't seem to be that much difference of opinion on whether two-tier energy pricing by the Government of Mexico or Pemex is a subsidy. The case was denied on the basis that we could not countervail or offset that subsidy under our law, because natural gas was sold to more than one specific industry in Mexico at the same price. I understand that the courts have recently reversed the basis for that ruling in the Mexican carbon black case.

As a businessman, it is clear to me that the marketplace would not set two different prices for natural gas sold by the same gas producer to competing industrial users; that is, a low price if you were a Mexican ammonia producer, and a higher price if you were a U.S. producer.

If the Government of Mexico owns all the oil and gas and controls all the production, has a monopoly on fertilizer and petrochemcial protection, and is the only entity authorized to export gas or ammonia or urea from Mexico, and sells natural gas at a lower price to its own industry, that is clearly discrimination, in my opinion.

If Pemex, as a matter of government policy, is given an unfair and artificial advantage as an ammonia producer, then it is simply unbeatable in the marketplace. The only difference in the gas price for Mexican gas sold in Mexico or exported to the United States should be its transportation costs.

If U.S. producers can't bid on the same gas at the same price, Pemex has an unfair advantage. It is one created solely by the Government of Mexico and not by any natural advantage that Mexico has in having greater reserves of gas than it can currently use in its own economy.

Mexico could clearly sell its excess gas to the United States at a much higher price than it is selling it for in Mexico. Mexico can certainly realize a better return on that gas by exporting it for a profit rather than flaring it. Mexico can make more by selling its gas to the United States than it can by turning it into ammonia and then exporting the ammonia.

What Mexico is doing just doesn't make any sense in the marketplace from the viewpoint of a businessman. This is the kind of discrimination and unfair trade practice that we are talking about here today.

Senator LONG. So far, those of you who come in here trying to save your industries and save the jobs, of for the workers who work for your industries, have not had much help from these so-called "macroeconomists" turned out by Harvard, Stanford, and other universities. And I am convinced that at some point you are going to find yourselves some economists who can bring ideas together and help you establish your case on the macroeconomic basis, on the overall aspects of it, because I am satisfied that it is a better case than is being presented. You fellows know what you are talking about when you talk about your business and talk about the American market. The other side has the backing of a lot of theoretical economists who have not had to meet the same payroll you have had to meet and don't have the same problems.

But from a philosophical point of view, their testimony sounds good, and some percent of it we don't have the right answer for, I'm sure.

This much does concern me when I hear them testify, that the free trade program that they seem to think is the greatest thing since sliced bread is leading us in a direction where we would go into debt at the rate of about a trillion dollars every 5 years to other foreign nations around the world.

Now, if you continue to advocate that philosophy of free trade, that would include a free flow of capital. That is implicit in the idea of free trade. And it would mean that the capital thus generated would go anywhere in the world that it could be used most effectively. But I don't see how the United States is going to make good over a period of 20 to 25 years. After 25 years you would be $5 trillion in debt to countries to whom this market is being made available while they are not doing the same thing for us.

Now, I can't see any answer down the road. Eventually, to make good the debts that we owe them, they would find it necessary to come over here and buy out our factories, our office buildings, a great deal of our real estate including farms, to make good the securities, the dollar securities or whatever debt we owe them. I think they wouldn't be well advised to leave that in terms of a dollar debt of the United States; it would be just too easy for the United States to pay it off with cash.

I think you heard me mention earlier that, if we keep running up the kind of debt we are talking about doing, eventually somebody is going to have to inflate our way out of the trap we would find ourselves in. And if I were them, I wouldn't let the United States owe me all that money in cash; it is just too easy to pay it in cash by saying, as I said before, "Would you like to be paid in dollar bills, or would you like to paid in million dollar bills, or would you like to be paid in billion dollar bills?" and then just print some.

One way or the other, this whole world trading system is going to come crashing down someday unless we find a way to move toward a balance. I don't think we can keep this thing up. Now we are running, say, a $150 billion deficit, and it will go to $200 billion in short order if we let the trend develop and continue that way.

Do any of you have any suggestions about this matter?

Mr. CALVERT. I could make a couple of comments.

Senator LONG. Yes, sir.

Mr. CALVERT. I have listened to these economists also. They all seem to give you this "on the one hand," and "on the other hand." While they are waving their arms around, we are going broke.

The other comment I would make: These philosophical arguments they give you—I wish they could figure out some way to take the unemployed people in this country and feed the arguments to them. Those folks don't have money to buy food. We have high unemployment in this country, and in my opinion it is unacceptable. We've got a $150 billion trade deficit, as you pointed out, that is also unacceptable. And these two things, as fer as I am concerned as a businessman, are the bottom line as to whether our trade laws and our trade policies are correct. And, by golly, they tell me they are incorrect.

Senator LONG. I heard what the chairman said about the Canadian timber, and I am not sure that I have the answer to it; but my inclination is to feel that if we are going to do business with Canada—and I'm all for it; I am for expanding trade between the United States and Canada—it ought definitely to be on a level playing field.

Now, our oil and gas people have discussed the idea of a common market with Canada, and one of them told it to me something like this: He said they were not opposed to a common market with Canada on oil and gas, if the Canadians wanted to do it; but he said, "If we do it, we would have to insist on a level playing field, and also that they play by the same rules. as we."

You know, up there they play football by our rules except they have 12 men on the playing field. We may have better ball players than they have, but I would be willing to bet that we can't beat a Canadian team with an 11-man American team. Another ballplayer on that field would kill you.

The people of Canada are neighbors of ours, they are good people, they can freely emigrate back and forth and we can freely move across their boundaries, and it is a wonderful relationship, and I am for making it stronger; but I would think that they could understand if we told them they are big boys now and that they have to play by the same rules we play by if we are going to engage in a common market with them.

If they are going to let their people have that timber at a much lower cost than we have to pay, then it seems to me as though the burden would be on our companies to make it available on public lands in the United States to meet that price, or else to take some other action to even the playing field up.

I discussed that with a Canadian negotiator at Geneva on occasion, and I indicated to him that it didn't seem right to me that they had that 8-percent manufacturers excise tax which was rebated at the border on products moving in our direction. We have a 7-percent Social Security tax matched by a 7 percent. workers' share.

As far as the businessman is concerned, if you are paying 14 percent in Social Security tax, it doesn't make much difference whether he pays half to the worker and half to the Government, or whether he pays it all directly to the Government. It all has to come out of his pocket; he is separated from all that money. And from a businessman's point of view, it doesn't make much difference whether you call it a "wage" or whether you call it a "tax"; he still has been relieved of that much money even though the worker was not able to go out and spend the money for himself.

Now, if they are going to unburden themselves of their taxes when they ship something in our direction, we ought to do the same thing.

This person on that occasion told me that he didn't think we ought to conclude a round of negotiations without bringing the subject up if we had any idea of doing the same thing to them that they are doing to us; that is, to change our tax system so we could rebate the tax on our exports the way they do, and also charge it as a border tax on their imports.

Do you see what I am talking about?

Mr. CALVERT. Yes.

Senator LONG. So, obviously, he wouldn't want us to do that; nobody in Canada would want us to do that. But you would then have a level playing field. You would have to adjust your tax system so that it would do the same type thing for your people as their system did for their businesses. Does that seem fair?

Mr. CALVERT. It seems fair to me.

Senator LONG. Well, that is just one of the many problems that we have where, if this Government simply wants to look the other way, you will watch a lot of businesses in this country go out of business, and a lot of workers lose their jobs, while other governments wouldn't do business that way.

I don't know any other nation that is willing to take the same attitude toward the dissolution of its basic industries that this Nation has been taking in recent years, and I am satisfied we can't keep it up.

Mr. CALVERT. I agree with you, Senator.

Senator LONG. Thank you very much, gentlemen, I appreciate your coming.

I want to put in the record some questions that Senator Bradley wanted to ask Professors Jackson, Aho, and Hufbauer, and he asked that they provide answers, if they can, before they leave town.

Thank you very much.

[The questions follow:]

Professor Hufbauer. Yes, sir.

[Whereupon, at 1:19 p.m., the hearing was concluded.]

[The following was received for the record:]

STATEMENT OF THE
AMERICAN INTERNATIONAL AUTOMOBILE DEALERS ASSOCIATION
REGARDING
UNITED STATES TRADE POLICY
BEFORE
THE COMMITTEE ON FINANCE
OF THE
UNITED STATES SENATE

Robert M. McElwaine,
President

American International Automobile
Dealers Association
1128 16th Street, N.W.
Washington, D.C. 20036

Bart S. Fisher, Esq.
Robert J. Portman, Esq.
Patton, Boggs & Blow
2550 M Street, N.W.
Washington, D.C. 20037

November 21, 1985

STATEMENT OF THE
AMERICAN INTERNATIONAL AUTOMOBILE DEALERS ASSOCIATION
BEFORE THE SENATE COMMITTEE ON FINANCE

The American International Automobile Dealers Association (AIADA) represents the interests of over 7,000 American automobile dealers and their 170,000 or more employees. AIADA is pleased to have this opportunity to participate in a review of U.S. trade policy. We feel strongly that the United States must continue in its traditional role as an advocate of free and fair trade. Reverting to protectionism in any form is not the solution to our current trade deficit. The imbalance is largely the result of macro- and microeconomic factors unrelated to U.S. trade law and cannot be resolved by erecting trade barriers. The views expressed below are consistent with the interests of our membership, but also consistent with the broader domestic and international interests of the United States.

Fair Versus Unfair Trade

United States trade law and policy is properly predicated upon a distinction between fair and unfair trade practices. Achieving a much-discussed "level playing field" necessitates consistent opposition to unfair trade and an open door to fairly traded imports. To abandon our leadership role as an advocate of a global system of free and fair trade is to roll back the tremendous progress which has been made since World War II in liberalizing world trade. We must avoid at all costs the building of national trade barriers and the kind of escalating protectionism which characterized the 1930's and ultimately destroyed the international trading system. As discussed in more detail in the second part of this testimony, our burgeoning trade deficit is not the result of unfairly traded imports. Larger macroeconomic shifts -- especially the overvalued dollar - are the major source of the current deficit. Lowering the value of the dollar, improving U.S. productivity and other measures, not protectionism, are necessary to redress the trade imbalance.

Pursuant to internationally agreed upon standards, the United States already combats unfairly traded imports, primarily through antidumping and countervailing duty laws, section 337 (for patent infringements and other unfair practices), and various customs fraud provisions. It is our view that, with respect to imports, these laws adequately cover the range of foreign governmental and corporate activity which can reasonably be described as "unfair."

The classic unfairly traded import is one which has received foreign government assistance in its production, marketing or export. Subsidies have the effect of pitting U.S. companies against the resources of foreign governments instead of the specific enterprises which compete in the same market. U.S. law already offers relief from subsidized imports which offsets the inherent unfairness of subsidization.1/ Similarly,

---

1/ With the exception of the United States, such subsidization has been on the upswing in the developed world since the 1950's. The relatively lower incidence of subsidies in the United States compared to its major trading partners is shown in attachment 1.

antidumping laws protect U.S. industries from imports sold at below costs of production or below the price such goods are sold in home markets. Again, relief offsets any effect of unfair pricing.

In keeping with international standards, the United States also combats unfair foreign practices that curtail U.S. export sales, artificially affect trade flows or violate trade agreements. Section 301, as amended in 1984, enables the United States to retaliate effectively against unfair practices of foreign countries that hinder U.S. exports. The Reagan Administration has recently shown a willingness to rely heavily on this provision to combat foreign barriers to U.S. goods. Three actions were initiated by the White House on September 7, and on September 23 an Administration task force was created to investigate unfair trade practices. A number of consultations are currently underway as a result of section 301 actions. Other unfair trade practices, many of which were identified in the October 20 report on foreign trade barriers prepared by the Office of U.S. Trade Representative (USTR), will be the subject of section 301 proceedings should bilateral negotiations fail to produce significant reductions in these trade barriers. To expand the scope of current unfair trade laws would be to violate carefully crafted GATT rules and abandon the essential distinction between fair and unfairly traded imports.

Relief for U.S. industry is even available in the absence of unfair foreign trade practices. Such relief is constrained by international rules which permit only limited responses to fairly priced imports. Under Article XIX of the GATT, countries are permitted to "escape" temporarily from their international and bilateral commitments to allow time for domestic industries adversely affected by imports to adjust. This relief is only for extraordinary circumstances and cannot, under long-established GATT principles, be made easily available. The United States has taken considerable advantage of this special exemption for economic adjustment. There are at least six different U.S. statutory responses to fairly priced foreign competition.

1) The "escape clause," contained in section 201 of the Trade Act of 1974;
2) Adjustment assistance to help firms, workers and communities harmed by the influx of imports;
3) Section 22 of the Agricultural Adjustment Act, which is designed to deal with problems caused by agricultural imports;
4) Section 406 of the Trade Act of 1974, which specifically addresses the issue of market disruption created by non-market economies;
5) Section 232 of the Trade Expansion Act of 1962, which is designed to limit imports which may impair national security; and
6) Import restraints on textiles permitted under the Multi-Fiber Arrangement (MFA) and the bilateral agreements negotiated by the United States pursuant to the MFA.

Of these safeguards, the broadest ranging and potentially most destructive to free trade is the escape clause mechanism found in section 201 of the Trade Act of 1974. This mechanism offers relief to U.S. industries when there is absolutely nothing unfair about the imports in question. Even so, section 201 has been attacked by those seeking less strenuous routes toward eliminating or handicapping aggressive import competition in the American market.

Claims that section 201 is not working ignore the recent history of the escape clause. A review of the cases the International Trade Commission (ITC) has decided during the past decade demonstrates that the Commission's determinations were correct and that the presidential discretion has been exercised, as it should be, with due regard to the general welfare of the nation.2/

Eleven cases have been brought before the ITC during the tenure of the Reagan Administration. Of these 11, the ITC found in six cases that import competition was not a significant cause of injury. Of the five remaining cases, the President imposed significant restrictions on the imported goods two times -- large motorcycles and specialty steels. In a third case -- carbon steel - he resolved the situation through the negotiation of voluntary restraints on steel imports.

In two cases, involving copper and footwear, the President rejected the ITC recommendations. In the case of copper, the Administration found that imposing restrictions on imported copper would eliminate more U.S. jobs in fabricating than it

---

2/ See attachment 2 which describes the results in section 201 cases between 1976 and 1983.

would save in mining. In the case of shoes, the President decided against the ITC recommendation on the grounds that protectionism would increase consumer prices without improving the competitive situation of the domestic industry. As discussed below, these decisions were made by the President in his unique role as protector of the broader national interest.

AIADA was a major participant in the 1980 ITC automobile decision -- perhaps the most famous of the recent escape clause cases. The action was brought by the Ford Motor Company and the United Auto Workers for relief from import competition from Japanese automobiles. AIADA participated in the long and arduous hearings and watched from an uncomfortably close position while the ITC wrestled with a complex factual situation and controversial political issue.

The ITC determination in that landmark case was eminently correct. The ITC had before it two unassailable facts: the U.S. automobile industry was facing severe economic difficulties, and Japanese automobile imports had increased significantly. The key issue, however, was whether Detroit's distress was due to imports or to other factors. After 46 hours of public testimony from 27 different groups over a week-long period, it was determined that increased imports were not a "substantial cause of injury," as defined in section 201, to the domestic industry. The economic conditions of the time and the change in consumer tastes to more fuel-efficient automobiles were found to be far more influential in causing the slump the Detroit automakers were experiencing.

The automobile case was proof of the efficacy of the escape clause action and the wisdom of the architects of that law.

Not surprisingly, those whose pleas for relief have been refused have cried, "We wuz robbed," and demanded that the entire escape clause system be dismantled and restructured. Efforts to shortcut the steps for relief under section 201 would seriously erode our international obligations and turn the "escape clause" rationale on its head: instead of limiting restrictions on fairly traded imports to special cases of economic adjustment necessitated by imports, section 201 would become a blunt instrument of protectionism.

Claims have been made that procedures followed by the ITC are too complex and time-consuming and that the burden of proof placed on the claimant is excessive. Critics have especially focused on the ITC injury determination, arguing that proof of injury should be automatic any time imports have achieved a greater market share over a certain period of time, or increased quantitatively. Such pleas to avoid an injury test ignore the seriousness of the ITC determination. The Commission is being asked to determine whether the government should interfere in the free workings of the marketplace by placing quantitative or pricing handicaps on one component of any industry, to the obvious benefit of another component of the same industry. Such action is contrary to fundamental American principles which hold that interference in the free operation of the marketplace is antithetical to the welfare of the nation. When the ITC recommends action and such recommendations are accepted by the President, the consumer inevitably pays more for goods and the choice of goods is narrowed.

Given the extraordinary consequences which flow from a positive determination, it is proper that a careful investigation be made of the health of the industry and the real effect of increased imports on that industry. In fact, were such relief from competition to become nearly automatic, our antitrust and price-fixing laws would be made a mockery. As noted above, such determinations also would violate multilateral and bilateral obligations and inevitably lead to retaliation by our trading partners. Absent price and quality competition, American goods would become over-priced and noncompetitive and high inflation would return to the American economy.

Another proposal involves amending the escape clause to require implementation of the relief recommended by the ITC unless the President refuses and the refusal is backed by a concurrent resolution of Congress. Robbing the President of his discretionary powers, which are already tempered by the possibility of a concurrent resolution and congressional override, would be detrimental to the U.S. economy and the international trading system. Currently, the escape clause establishes a two-tier process in which the ITC acts as a fact-finder and the President acts as a policymaker. In its fact-finding role, the Commission evaluates the economic condition of the domestic industry and the causal effect of increased imports. If injury and causation tests are met, the ITC recommends adjustment assistance or global import restraints. Then, in his policymaking role, the President evaluates whether the ITC recommendation is in the overall national interest.

Among other things, the President must take into account the efficiency of import controls in promoting industry adjustment, the cost to consumers, the likely retaliation by foreign trading partners, the economic and social costs involved, and the international economic and foreign policy interests of the United States. By taking away the President's policymaking power, consideration of broad-ranging national and international concerns would be eliminated. As a result, U.S. trade policy would become overly responsive to narrow industry-specific interests, to the detriment of overall national interests.

What is needed is not reform of section 201 but enhanced internationalization of its standards. At the upcoming round of the GATT, the United States should promote a new "safeguards" code to regulate the means by which GATT members can lawfully limit imports. This is a key bit of unfinished business from the 1974-1979 Multilateral Trade Negotiations exercise. A new safeguards code should address the appropriate injury standards for the granting of "escape clause" relief, compensation for affected exporters, consultation procedures and most favored nation-related issues.

Section 201 has a proven track record as a mechanism which works to provide appropriate relief in extraordinary situations.

Going beyond the current provisions would be contrary to our international obligations and would open the door to protectionism in response to fairly traded imports. It is a classic example of a procedure that "ain't broke" and, thus, should not be fixed.

Resolving the U.S. Trade Imbalance

The question might be asked: If U.S. fair and unfair trade laws are working, then why are we running such a large trade deficit and why are major U.S. industries losing markets to foreign competition? The answer is that the current trade deficit is not a result of unfair trade but primarily due to macro- and microeconomic factors which are not affected by U.S. trade law. The most important macroeconomic factor affecting the U.S. trade balance is the high value of the dollar relative to the currencies of our major trading partners. The rise in value of the dollar is the primary reason for the poor performance of U.S. exports. Some have asked whether the fallen dollar will improve the nation's trade balance. This is the economic equivalent of asking whether water will flow downhill. The recent history of the imported automobile industry demonstrates the fundamental interrelationship between exchange rates and international trade.

In 1971, President Nixon closed the gold window and shortly thereafter initiated an era of floating exchange rates. Released from its artificially high fixed price, the dollar fell like a stone against stronger currencies, particularly the German mark. Sales of Volkswagens, then the dominant imported automobile, had reached 575,000 units in 1971. By 1974, this number fell to 334,000 units, then to 200,000 in 1976 and below 100,000 in 1980.

In 1978, the dollar declined steadily throughout the year against the yen, largely due to worsening inflation in the United States and lack of confidence in the U.S. economy. During that year, Japanese automakers instituted five price hikes to cover their declining dollar revenue from yen/dollar transactions. As a result, sales of Toyota automobiles, for example, fell from 493,000 in 1977 to 442,000 in 1978. The decline in Japanese auto sales would have been far more precipitous had not the domestic manufacturers matched the Japanese exchange-rate-induced price hikes almost dollar-for-dollar. In the beginning of 1979, inventories of Japanese cars had reached saturation levels, as buyer resistance to higher prices began to build. Only the explosive demand for fuel-efficient automobiles following the fall of the Shah and the second oil crisis of 1979 enabled the Japanese automakers to weather the higher prices forced on them by the weaker dollar.

Today, the depreciation of the dollar, which has been ongoing since its peak value in February 1985, is speeding up. The September 22 Treasury Department intervention in world currency markets was an indication of the Administration's commitment to continue efforts to bring down the value of the dollar. Already, the dollar is approaching the lowest value it has held against the yen during the post-War period. From a high of 269 yen to the dollar in the spring, the dollar has fallen to 205 yen in November. Predictions are that it will settle around 200 and may fall as far as 190 yen.

Again, the impact of the lower dollar on the imported automobile industry is revealing. First, one must understand the procedures by which the U.S. distributing arms of Japanese manufacturers obtain their product. U.S. distributors use the dollars they earn from vehicle sales to dealers to buy yen on the open market. They engage heavily in futures purchases to flatten out severe exchange rate fluctuations. The cars they order from the Japanese manufacturer are paid for in yen. Thus, the price the distributor pays for yen is critical to the profit margin.

Consider the case of a Japanese automobile selling at a wholesale price in Tokyo of 2 million yen. In the spring of this year, when the yen stood at 269 to the dollar, it took $7,435 for the U.S. distributor to pay for the car by acquiring the needed yen. By late summer, when the yen had risen to 250 to the dollar, the same car, at the same price in yen, cost $8,000. Again, at 205 yen to the dollar, that same car, without any increase in factory price, costs the distributor $9,756. That represents an increase of $2,321, or more than 30 percent, in a little more than six months.

To date, the Japanese manufacturers have managed to absorb this differential without disruptive price increases, since their cars have generally been priced on the assumption of 220 yen to the dollar exchange rate. Obviously, the present price structure cannot continue to hold if the yen remains in the neighborhood of 200 to the dollar. As a result, price increases after January 1 are expected.

The domestic manufacturers, on the other hand, instituted significant price increases in October, with the introduction of 1986 models. When couched in manipulated percentage terms, the Detroit price hikes did not seem extravagant. When one studies the actual effect on transaction prices, however, it becomes apparent that the American automakers have, by such devices as making formerly optional equipment standard, raised the selling price of their product by a substantial margin. On some larger General Motors models, the sticker price has gone up by as much as $2,000. Add to this increase the effect of the end of subsidized 7.5 percent U.S. automobile financing (which increased costs by $1,000 for some customers) and you have price hikes of a magnitude sufficient to halt a sales boom in its tracks. It has been speculated that the domestic manufacturers, anticipating price increases by the Japanese, decided to cover that expected boost in price at the time of the new model introduction, thus avoiding the embarrassment of raising their prices after the Japanese.

The announcement by the U.S. Department of Commerce on October 31 that the September merchandise trade deficit was $15.5 billion, a record monthly high, seems to run counter to the theory that a declining dollar reduces the trade deficit. On closer inspection, however, the September trade figures are an unreliable and even misleading indicator. One reason is that depreciating currency may initially increase the trade deficit as prices of exports and imports adjust more rapidly than do trade volumes. This phenomenon, known as the "J-curve," has recently been documented by Professor Charles Pearson in a study for AIADA entitled "Trade Deficits and the Dollar: A Cautionary Note." A copy of this paper is appended as Attachment 3. It may be helpful to illustrate the "J-curve" by an example taken from U.S. automotive trade with Japan.

Shipments of automobiles from Japan rose substantially in September over the year-earlier figures, both in numerical terms and in dollar value. The dollar-value figures, however, were subtantially distorted by the fall in the dollar. The increase in value is recorded at $533 million. Virtually half of this increase can be accounted for by the abrupt change in the yen/dollar exchange rate.

The vehicles in question were paid for in Japan with yen bought at least three months, and perhaps as much as six months, earlier. The United States Customs Service, however, evaluates such shipments on the basis of landed value -- in dollars -- at the time of importation. Consequently, the trade figures for September will show the value of incoming Japanese vehicles as $270 million more than was actually paid for them. Such distortions commonly accompany rapid changes in exchange rates. The higher values of September imports should not be regarded as an unhealthy sign, but rather as an indication that the fever has broken and the patient is beginning a recovery.

The high value of the dollar is perhaps the major cause of the U.S. trade deficit. The exchange rate intervention by the five major industrial countries we have seen in the past several weeks is a positive sign. Additional efforts on the part of the developed countries to coordinate their monetary and fiscal policies are necessary to resolve the problems of our poorly functioning international trade system. But we also have a responsibility to act at home to reduce our burgeoning budget deficit which acts to keep the dollar at a high value.

Not all of our trade imbalance can be laid at the doorstep of the high dollar: Another reason is the reduced demand for U.S. goods by less-developed countries which are under heavy debt burdens. There are also microeconomic factors at work which make U.S. goods uncompetitive in world markets. U.S. productivity is lagging. Between 1977 and 1983, productivity grew at a rate of 1.2 percent per year in U.S. manufacturing. This was one-half Germany's growth rate (2.5 percent), one-third the French rate (3.5 percent), and less than one-third the Japanese rate (3.9 percent).3/

3/ Lester Thurow, "America, Europe and Japan," The Economist, November 9, 1985.

Conclusion

In the press release announcing these hearings, Chairman Packwood is quoted as saying he is "concerned that we are not realistically facing up to the challenges of 'fair trade.'" We share this concern: Current trade laws provide adequate relief for unfair foreign practices. However, we must look beyond trade law in responding to fairly traded competition. Reverting to protectionism would be a disaster; it would drive domestic prices up, causing inflation; it would weaken the long-term competitiveness of U.S. industry; it would invite retaliation; and, given its current fragility, it could lead to a general breakdown in the international trading system.

Keeping out certain foreign goods to protect selected U.S. industries is not a solution to our trade imbalance. The United States, preferably in conjunction with its major trading partners, must face up to the macroeconomic causes which distort international trade patterns. In particular, coordinated efforts already begun to intervene in foreign exchange markets to bring down the value of the dollar should be continued. It is through such efforts, not the creation of new barriers to trade, that the trade deficit can be reduced and the chances for long-term prosperity improved. U.S. industry must also become more competitive in the world marketplace. As the world economy is becoming increasingly integrated, the United States must continue to stand up for free trade. By addressing the real causes of the U.S. trade deficit, we can be active participants in a free and fair international trading system.

ATTACHMENT 1

Investigation	Product	Date of Investigation	Duty on Product in Effect in Year of Investigation	Existing Quantitative Restriction on Product	Determination of ITC	Recommended Relief of ITC	Relief Granted By President
TA-201-4	Asparagus	Jan. 76	Col. 1 Col. 2 Fresh: 25% 50% ad val. ad val. Canned: 17.5% 35% ad val. ad val.	None	Commission Equally Divided	5-year quantitive restriction declining after third year	None
TA-201-10	Mushrooms	March 76	3.2 cts per lb + 10% ad val. (rate fluctuated periodically from June 18, 1930)	None	Affirmative	Adjustment Assistance (3 commissioners) Quota, allocated on country by country basis; 3.2 cts/lb & +35% ad val. duty on over quota imports in first 3 years, +25% ad val. in 4th year, +15% + in 5th year (1 commissioner)	Expedited Adjustment Assistance
TA-201-12	Shrimp	May 76	Duty free	None	Affirmative as to shrimp fishing industry (negative as to shrimp processing industry)	Adjustment Assistance	Expedited Adjustment Assistance
TA-201-17	Mushrooms	Jan. 77	Col. 1 Col. 2 3.2ct/lb +10% ad val. 10ct/lb +45% ad val.	None	Affirmative	Tariff-rate-quota system for 5-year period; Quota allocated in country-by-country basis-Tariff over quota decreasing in 4th & 5th years (3 Commissioners Adjustment Assistance (2 Commissioners)	Monitored Imports; ITC Quarterly Reports
TA-201-22	Fresh Cut Flowers	Aug. 77	Col. 1 Col. 2 10% ad val. 40% ad val.	None	Negative	None	None

TA-201-25	Live Cattle & Certain Edible Meat Products of Cattle	Sept. 77	Col. 1 Between 1.5 ct/lb and 2.5 ct/lb depending on weight Col. 2 Between 2.5 ct/lb and 3.0 ct/lb depending on weight	None	Negative	None	None
TA-201-40	Leather Wearing Apparel	Jan. 80	Duty Free: On GSP list of eligible products Jan. 1, 1976-March 1, 1979	None	Affirmative (as to coats and jackets only)	Increased tariff 25% ad val. 1st year 20% ad val. 2d year 15% ad val. 3d year	Adjustment Assistance
TA-201-41	Certain Fish	Jan. 80	N.A.	None	Negative	None	None
TA-406-6	Anhydrous Ammonia	April 80	Duty Free (except small quantities: 6.4% ad val. (col. 1); 20% ad val. (col. 2)) (GSP eligible)	None	Negative	None	None
TA-201-42	Fresh cut Roses	April 80	Col. 1 8% ad val. Col. 2 40% ad val (not GSP eligible)	None	Negative	None	None
TA-201-43	Mushrooms	August 80	Col. 1 3.2 ct/lb + 10% ad val. Col. 2 10 ct/lb + 45% ad val.	None	Affirmative	3-year quantitive restriction; decreasing in 2d and 3d years	Additional tariffs for 3 years: 20%, 15% and 10% ad val. in 1st, 2d & 3d years respectively
TA-201-44	Motor Vehicles	Dec. 80	Col. 1 2.9% ad val. to 8.5% ad val. Col. 2 10% ad val. to 25% ad val. depending on type and weight	None	Negative	None	None
TA-201-45	Fishing Rods & Parts thereof	Nov. 81	Col. 1 14.3 ad val. (decreasing to 7.6% ad val. by 1987) Col. 2 55% ad val.	None	Negative	None	None

TA-201-46	Tubeless Valves	Sept. 82	Col. 1 3.7% ad val. (decreasing to 3.1% ad val. by 1987 (GSP eligible) Col. 2 25% ad val.	None	Negative	None	None
TA-406-9	Mushrooms from PRC	Sept. 82	Col. 1 3.2 ct/lb & 20% ad val. (decreasing to +15% ad val. in 1981 and to +10% ad val in 1982) Col. 2 10 ct/lb + 45% ad val.	Quantitative restrictions for a 3-year period	Commission equally divided	None	None
TA-201-47	Heavyweight Motorcycles	Feb. 82	Decreasing between 1983-1987 from 4.4% to 3.7% ad val., 2.0% ad val. to free; 3.6% to 3.1% ad val., or 52% ad val. to 4.2 ad val., depending upon type and weight	None	Affirmative	5-year tariff increase, decreasing from 45% ad val. in 1st year to 10% ad val. in 5th year	ITC relief adopted and tariff rate quotas adopted in addition (See Attachment 1)
TA-201-48	Stainless Steel & Tool Steel	May 83	Col. 1 Between 4.2% ad val. and 11.5% ad val. depending upon type (+ additional duties of up to .4% ad val. depending upon alloy content) Col. 2 Between 11% ad val. and 31% ad val. depending upon type (+ additional duties of up to 1% ad val depending upon alloy content)	None	Affirmative	Quantitative restrictions for 3-year period; added duties for other products	Additional tariffs for 4 years, declining each year on some products; global quotas on other products

ATTACHMENT 2

Subsidies as shown in national account statistics as a percentage of GDP[a]

Country	1952	1956	1960	1964	1968	1972	1976	1980
Italy	0.59	1.30	1.51	1.23	1.67	2.29	2.60	3.01
France	1.71	2.71	1.62	2.03	2.62	1.99	2.65	2.51
Canada	0.41	0.39	0.51	0.85	0.57	0.53	1.73	2.34
United Kingdom	2.68	1.76	1.93	1.56	2.06	1.52	2.78	2.32
Germany	0.65	0.20	0.79	0.99	1.44	1.48	1.49	1.59
Japan	0.79	0.26	0.34	0.65	1.11	1.12	1.32	1.32
United States	0.11	0.20	0.25	0.44	0.50	0.59	0.34	0.43

Source. OECD, *National Accounts 1951–1980*, vol. 1, Main Aggregates, 1982.
a. Countries listed in order of amount of subsidies as a percentage of GDP in 1980.

Source: Hufbauer and Erb, Subsidies in International Trade (Institute for International Economics; Washington, D.C., 1984), at p. 3.

ATTACHMENT 3

Trade Deficits and the Dollar:
A Cautionary Note

Prepared for
American International Automobile Dealers Association

November 1985

Charles Pearson
Professor of International Economics
School of Advanced International Studies
Johns Hopkins University

On October 31, 1985 the U.S. Department of Commerce announced that the September merchandise trade deficit was $15.5 billion, up from $9.9 billion in August. On the surface this appears deeply disturbing. Not only was the September trade deficit at a record monthly high, but the increase occurred despite a decline in the value of the dollar that started in February 1985. Everything else equal, a declining dollar is thought to reduce a trade deficit.

On closer inspection, however, the September trade figures prove to be an unreliable guide, and other evidence suggests that the U.S. trade position may stabilize and subsequently improve. The more sanguine interpretation rests on analyses of how the trade data are compiled and reported, the so-called J curve effect, and empirical studies that tend to confirm the responsiveness of trade flows to real exchange rate changes.

Monthly Trade Statistics

Little meaning can be attached to the September trade deficit itself. There are four reasons. First, the Commerce Department is required by law to initially release trade data that measure export values F.A.S. (free alongside ship) and import values C.I.F. (cost, insurance, freight). Thus, imports include freight charges and exports exclude freight charges and the two are not directly comparable. After 48 hours, the Commerce Department is permitted to release import values on a customs basis, excluding freight charges. On a customs basis, the September trade deficit was $14.0 billion, $1.5 billion lower than initially reported.*/

Second, month-to-month variation in trade balances can be substantial. Average variation of the monthly balances has been $1.7 billion over the past year. Moreover, the August trade deficit of $8.7 billion (F.A.S. exports, Customs imports) was unusually low, with the preceding three month average at $10.8 billion. The Commerce Department itself recommends caution in interpreting monthly charges: "Cumulation of data over at least 4 month periods is desirable to identify underlying trends. Month-to-month charges in exports, imports, and similar series often reflect primarily irregular movements, differences in monthly carry-over, etc."**/

The monthly average merchandise trade deficit (exports F.A.S., imports customs) was $10.4 billion for February-May 1985 and $11.0 billion for June-September, a 6% increase. In contrast, the trade deficit grew 75% between 1983 and 1984. Thus the trend in the deficit is decelerating.

Third, the Commerce Department also reports "revised statistical month data" in which records are grouped and totaled by their transaction's dates. For example, the statistical month reports the August 1985 trade deficit (exports F.A.S., imports customs basis) at $9.9 billion, whereas the revised statistical month data show the August deficit to be $12.9 billion. With revisions of this magnitude, the initially reported September deficit becomes unreliable.

---

*/ For balance of payments reporting, earnings and expenditures on freight show up in services trade, not merchandise trade.

**/ U.S. Department of Commerce, Bureau of the Census, FT 900-85-09, p. 5, November 4, 1985.

Fourth, the Commerce Department sets as a cutoff date for information from Customs the 15th of the subsequent month. A large and varying fraction of the month's trade transactions remain unreported by the 15th (up to 58% of total transactions), and thus the monthly trade data depend in large part on how prompt or tardy the Customs Service is. Recent analysis by Census shows "the level and volatility of the carryover, particularly with respect to imports, has reached a magnitude that not only necessitates greater caution in interpreting month-to-month changes, but also requires a change in methodology. . ."*/ The uncertainty about the accuracy of the trade data has led the Department of Commerce, Bureau of Economic Analysis, which publishes trade data on a balance of payments basis, to postpone indefinitely trade data scheduled for release on November 8 and December 16, 1985 pending receipt of revised export and import data for July-September from Census.

For all these reasons the September trade deficit has little meaning in and of itself.

---

*/ Department of Commerce, Bureau of Census, FT 900-85-09, November 4, 1985, p. 2.

J Curve Effect

Since the dollar devaluation of 1971, economists and financial reporters have recognized the possibility that a depreciating currency may initially _increase_ the trade deficit as prices of exports and imports adjust more rapidly than do trade volumes.*/ As a result, the trade deficit may describe a "J-Curve", initially worsening but ultimately improving.

The concept is simple enough. If import contracts are at a fixed foreign currency price and the dollar then depreciates, the import price in dollars, as the goods clear customs, goes up, and the trade deficit, expressed in dollars also rises.**/ If the foreign currency price of exports declines by the amount of the depreciation, the dollar price of exports remains the same and there is no corresponding short run improvement in the value of exports. Over time, however, the increased price of imports leads to a decline in import volume, and when the volume effect outweighs the price ffect, the value of imports starts to fall. The adjustment, however, requires that the foreign seller does not absorb the exchange rate change, but passes some or all along in price increases. On similar fashion, over time the lower foreign currency price of exports leads to an increased volume, and the value of exports starts to rise. Thus, the possible J-Curve path for the trade balance.

---

*/ See for example William Branson, "The Trade Effects of the 1971 Currency Realignments," _Brookings Papers on Economic Activity: I_ (1972) and Stephen Magee, "Currency Contracts, Pass-Through and Devaluation," _Brookings Papers on Economic Activity: I_ (1973). Magee also shows that the trade balance may describe a "W" curve over time as trade passes through a "contract" period, a "pass through" period in which price changes are passed on to consumers, and a volume adjustment period. Takacs and Wilson take this one step further by showing that expectations of exchange rate movements may affect export and import decisions, thus magnifying the J curve effect. See Wendy Takacs and John Wilson, "Expectations and the Adjustment of Trade Flows Under Floating Exchange Rates: Leads, Lags, and the J-Curve," International Finance Discussion Paper No. 160 (Washington, D.C.: Board of Governors of the Federal Reserve System, April 1980).

**/ For example, if a Japanese car is contracted for at 2,500,000 Yen ($10,000) when the exchange rate is 250 Yen/$, and the dollar falls to 200 Yen/$, the dollar price at Customs is $12,500, an increase of 25%.

Two points should be made. First, the J-Curve effect should be welcomed as evidence that foreign sellers are indeed increasing import prices in the U.S. market, rather than absorbing the exchange rate change in profit margins, and that U.S. exporters are passing on a significant fraction of the change in lower foreign currency price for exports. Without these pass-throughs of price changes, trade volumes would not change, and there would be no long-run correction to the trade deficit.

Second, even if U.S. export prices in foreign currencies do not decline, the imbalance between the value of U.S. exports and the value of U.S. imports would produce a J-Curve. A 20% increase in U.S. import price and a 20% increase in U.S. export price (in dollars), holding volumes constant, would produce an initial deterioration of $28 billion.

Evidence in the current J-Curve remains thin. By late October 1985 the dollar has fallen by more than 16% on a trade weighted basis compared to its short-lived peak in February 1985. On a bilateral basis it has fallen 25% against the British pound, 23% against the German mark and 18% against the yen.

An examination of U.S. import and export price indices suggests, but does not conclusively demonstrate, the J-Curve effect (Table 1). As expected, the dollar price of U.S. imports of manufacturers was falling during December-March 1985, when the dollar was still strengthening. By March-June 1985, the dollar price of imports started rising as the dollar depreciated from its February 1985 high. The dollar price increase accelerated in the most recent period, June-September 1985, which again is consistent with the J-Curve hypothesis. Export price movements for manufacturers were mixed, but more modest than import price changes. This again is consistent with the J-Curve effect, which suggests a decline in foreign currency price of exports and stable dollar price of exports.*/

If the J-Curve effect proves substantial, some further deterioration in the trade balance may be expected. To the extent the decline represents price changes that will lead

---

*/ The analysis is restricted to manufactures, excluding chemicals. Food, crude materials and fuels prices are declining on a world-wide basis.

TABLE 1

Percent Change in Imported
Export Prices

	Dec. 1984 to March 1985	March 1985 to June 1985	June 1985 to Sept. 1985
Imports			
Manufactures, simple average	-2.3	+0.5	+1.3
Intermediate mfg. products	-2.7	-0.5	+0.9
Machinery & Transport	-1.3	+1.0	+0.9
Misc. Manuf. Products	-3.0	+1.0	+2.0
Exports			
Manufactures, simple average	-0.1	+0.4	0.0
Intermediate mfg. products	-1.0	-0.2	0.0
Machinery & Transport	+0.6	0.5	0.1
Misc. Manuf. Products	+0.2	0.9	-0.1

Source, U.S. Department of Labor, BLS, U.S. Import and Export Price Indexes, Third Quarter 1985, Oct. 31, 1985 to favorable volume changes in exports and imports, there is no reason for alarm. Note also that trade also responds strongly to economic activity in the U.S. and abroad, and the income effect on exports and imports may conceal the J-Curve effect.

Trade Response to Real Exchange Rate Changes

Some observers caution that recent and prospective declines in the real exchange value of the dollar will have minimal effect on trade values if foreign exporters absorb the depreciation through lower foreign currency prices (and lower profits). Two recent empirical studies, at the industry level, cast light on this question. Both studies provide grounds for modest optimism.

Daniel Citrin analyzes the response of Japanese exports to changes in the yen exchange rate for five products, all of which are sensitive U.S. imports -- subcompact passenger cars, color television sets, galvanized steel sheet, heavy steel plate and tin plate.*/ A hypothetical 10 percent appreciation of the yen was simulated for each product. The simulation shows that a portion of the 10 percent appreciation is absorbed by lower yen prices for exports (e.g. 5.2% for subcompact cars, 3.4% for heavy steel plate) but a portion is passed on to the foreign consumer. Export price adjustments are quite rapid. Export volume falls 10.8% for autos and 14.7% for color televisions, and by lesser amounts for the other products. Three-fourths of the response in export shipments occur within the first year for all five products.

---

*/ Daniel Citrin, "Exchange Rate Changes and Exports of Selected Japanese Industries", IMF Staff Papers, Vol. 32 No. 3, September 1985.

While the incomplete passthrough into foreign currency price increases and substantial lags in both supply and demand suggest that recent appreciation of the yen toward the 200 yen-dollar rate will not have immediate and maximum effects in reducing Japanese exports, the analysis does show long-run declines in export volume for all five products as a result of yen appreciation. This result suggests some reduction in Japanese export pressume in the U.S. market.

The second analysis, by Eric Clifton, analyzes the effects of industry specific real exchange rates on import penetration ratios (the ratio of imports to total consumption) for four industries (textiles, clothing, iron and steel, transportation equipment) for three countries, including the United States.[*/] The results for the U.S. show that the real exchange rate for the dollar is a significant positive determinant of the import penetration ratio in each industry. This suggests that exporters to the U.S. do indeed pass through price declines

---

[*/] Eric Clifton, "Real Exchange Rates, Import Penetration, and Protectionism in Industrial Countries", IMF Staff Papers Vol. 32 No. 3, September 1985.

when the dollar is rising and pass through price increases when the dollar is falling. Thus, the long period of dollar appreciation from 1979 through February 1985 has led to significant increases in import penetration ratios (and protectionist pressure). One might expect some stabilization and reversal of import penetration as the dollar declines. The mean lag for adjustment ranges from 1.5 quarters (clothing) to 8.5 quarters (transport equipment). The long-run elasticity of responsiveness of this import penetration ratio to the real exchange rate (i.e., the percent change in import penetration divided by the percent change in the real exchange rate for the dollar) is 0.2 for transport equipment.

Summary

No one disputes that the U.S. has a serious merchandise trade deficit. But closer inspection reveals (1) the September trade deficit, by itself, has little meaning, (2) the rate of growth of the deficit has slowed sharply since 1984, (3) some of the current and prospective near-term deficit may be the result of the J-Curve effect, which is to be welcomed, (4) recent empirical studies tend to confirm that Japanese exports respond negatively to a yen appreciation, (5) import penetration ratios in sensitive industries in the U.S. have, until recently, increased due to the strong dollar, and may decrease as the effects of a weaker dollar are felt.

One should also recognize that the actual trade deficit for 1986 will depend not only on exchange rates, but also economic growth in the U.S. and abroad. At a more fundamental level, it should be recognized that the cause of the U.S. trade deficit is the unbalanced macro-economic position of the country, including the large budget deficit, and that restrictive trade policies would be inappropriate and ineffective.

STATEMENT OF

PAUL T. MURPHY

VICE PRESIDENT

NATIONAL FOREIGN TRADE COUNCIL, INC.

BEFORE THE

SENATE COMMITTEE ON FINANCE

OVERSIGHT HEARING ON

UNITED STATES TRADE POLICY

NOVEMBER 21, 1985

The National Foreign Trade Council, an association of over 550 U.S. companies engaged in international trade, welcomes this opportunity to present its views on import competition and the trade deficit.

Even while the overall economy and U.S. employment continue to expand, intensified import competition has created difficult adjustment problems for many sectors of our economy. This is particularly true for traditional manufacturing industries, but the problem extends as well to some of the newer high-technology industries.

The dramatic increase in imports over the past several years-from $245 billion in 1980 to $325 billion in 1984--a gain of over 30%, together with a series of record trade deficits, requires thorough public discussion and an effective response to the number of important policy issues it raises.

Import Policy

A question which has assumed prominence as the trade deficit has mounted is whether increased import restrictions constitute an effective U.S. response to import competition. An unprecedented number of bills have recently been introduced in Congress calling for new import quotas, for import surcharges, and for amendments to the trade remedy laws which would permit additional restraints on imports.

The National Foreign Trade Council supports vigorous enforcement of existing trade remedy laws, i.e., the anti-dumping and countervailing duty statutes, sections 301 and 201 of the Trade Act, and other laws which provide for import curbs as a means to combat unfair trade practices of our foreign competitors or surges in fairly traded imports which cause major dislocations in particular sectors. These U.S. laws are consistent with an international consensus reflected in the General Agreement on Tariffs and Trade on what constitutes unfair trading practices and under what circumstances safeguard actions directed against fairly traded imports are appropriate. Statutes on unfair trade, in particular, can and should be used in a manner consistent with an open trading system by bringing dicipline to that system. Although we believe that these laws should be reviewed to see if improvements can be made in terms of administrative efficiency, we support the trade remedy laws substantially in their present form because they impose a degree of discipline on foreign competitors engaged in unfair practices and because they provide U.S. producers with breathing space--that is, with time to adapt to new competitive conditions. At the same time, sections 301 and 201 strike a balance between the rights of U.S. petitioners and other national economic or political interests.

We caution, however, against placing undue reliance on these laws, or in the name of fairness expanding the trade remedy laws to impose still more restrictions on imports. Import restraints can facilitate adjustment but do not in themselves foster competitiveness or constitute a program for sustained economic growth.

Indeed, import restrictions, whether imposed through tariffs, the trade remedy laws, or voluntary restraint agreements, impose very significant costs on the U.S. economy.

First, they contribute to inflation by increasing the costs of imports;

Second, they contribute to higher domestic product prices by lessening competitive constraints;

Third, they reduce the flow of imports from developing countries, thereby lessening the ability of those countries to purchase U.S. exports, and in the case of heavily indebted countries, to repay their debts;

Fourth, they provoke imitative or retaliatory measures by our trading partners, impeding U.S. exports;

Fifth, direct costs far exceed the gains; benefits flow to a sheltered industry at a high cost to the public. Some economists have estimated, for example, that the relief sought by footwear manufacturers in their Section 201 petition would have cost consumers approximately $50,000 per year for each job saved;

Sixth, import restrictions can do little to stem the tide if a decisive change in comparative advantage is under way. Such changes frequently occur, as developing countries with low labor costs or access to plentiful raw materials successfully adopt manufacturing technologies formerly held by industrialized countries;

Seventh, they act as a tax on a highly competitive part of the American economy, the export sector, by pushing up the value of the dollar and by raising input costs which exporters have difficulty in passing on, in a highly competitive world market.

Finally, import restrictions shelter U.S. producers in the domestic market but do not shelter U.S. producers competing in overseas markets.

Positive Contributions of Imports

Although the recent rise in imports reflects a disturbing decline in the competitiveness of some segments of U.S. industry, it should be noted that imports have contributed to the general health of the U.S. economy in the following ways:

- -- by helping to contain inflation;
- -- by helping to make U.S. industry more competitive in order to meet foreign competition on product price and quality;
- -- by contributing to the stability and growth of the economies of nations which sell their products to us and by providing the foreign exchange which these nations need to make purchases from us;
- -- by providing raw materials and finished products which the United States does not produce in adequate amounts (for example, petroleum).

While these positive aspects of imports may seem self-evident, we think it important to emphasize them because there is widespread public perception that imports are harmful to U.S. industry and provide no offsetting benefits. This perception is largely erroneous; imports play an important role in U.S. economic growth, and policies aimed at a substantial reduction of imports will inevitably impede that growth.

Recommendations

While import policy is an essential part of the U.S. response to our chronic trade deficits, other aspects of U.S. international economic policy have a more fundamental role. In addition to vigorous enforcement of our trade laws, we recommend a comprehensive response to foreign competition that consists of these elements: first, a reduction in the value of the dollar; second, policies and programs to enhance the competitiveness of U.S. industry; third, a major effort by the United States to reduce foreign and domestic barriers to U.S. exports; fourth, action to strengthen the institutions and the rules of the international trading system for goods and services; and fifth, action to induce the major industrialized countries to accelerate growth and absorb a greater share of world industrial output.

The Strong Dollar

A principal cause of the surge in imports and the trade deficit is the strength of the dollar.

While recent months have seen a decline of about 20% in the dollar from historic highs, today the dollar has been characterized by many economists as still overvalued on a trade-weighted basis. While slower growth rates abroad are also a factor, the huge U.S. trade and current account deficits are in very significant part the result of this currency imbalance.

Accordingly, our first recommendation to address the problem of import competition is that the Administration and Congress work together to reduce the federal budget deficit. Smaller deficits would reduce the Treasury's borrowing needs, leaving more credit available for private investors, thereby effecting a reduction in interest rates and in the attractiveness of the dollar to foreign investors. A continuation of the present downward movement of the dollar would help U.S. products over time to become more price competitive in the domestic and international markets. Even if the current budget impasse is resolved by Congress, very substantial additional budget reductions must be made in the next several years to impose controls on runaway expenditures.

U.S. Competitiveness

We caution, however, that even a significant further reduction in the value of the dollar against the currencies of our major trading partners would not, in and of itself, eliminate the trade deficit or the price advantages of imported products. Many foreign competitors are so dependent on exports to the U.S. market that they would absorb price reductions resulting from a decline in the value of the dollar in order to preserve market share. Moreover, in many cases, our foreign competitors can count on their comparative advantages in production efficiencies or in low labor or raw materials costs. Unless the productivity of U.S. industry increases more rapidly, the advantage resulting from a dollar decline will be insufficient to enable many segments of U.S. industry to meet international competition over the long term. During the past eight years, annual productivity growth in the United States has averaged 0.7% compared with Western Europe's 1.8% and Japan's 3.4%. To sustain an acceptable growth rate of our gross national product and meet intensified international competition, it is essential that U.S. industry step up its efforts to enhance productivity and that our government maintain policies which will encourge efficiency and innovation. These policies should be directed toward three main objectives: ensuring that an adequate supply of savings is available to finance industrial expansion and innovation, at a reasonable cost; providing incentives for technological innovations; and maintaining an educated and adaptable work force.

With respect to financing industrial expansion, reduction of the Federal budget deficit would result in lower interest rates and lower costs for industrial capital. Tax policies should be directed toward encouraging savings and providing incentives for risk capital, and enhancing, not impeding the competitiveness of U.S. industry.

With respect to technological innovation, the United States must maintain leadership in science and technology because it is experiencing increasing difficulty in matching the relatively low labor and raw materials costs of developing countries which are quickly acquiring the techniques of mass production--for example, in textile and steel manufacture. For a number of years, U.S. business has been shifting toward higher technology products and services, in which the United States has a relative advantage. This competitive response, accompanied by restructuring of a number of America's basic industries, must be accelerated through tax and other incentives for increased research and development and policies which stimulate innovation and leadership in science.

The third ingredient is an educated and adaptable work force. The need for more science and engineering graduates, for example, has been widely publicized. The number of functionally illiterate Americans is astonishingly high. The Federal adjustment assistance program which has functioned in large part as a system to provide supplemental unemployment benefits has, overall, not successfully addressed the problem of displaced workers. U.S. corporations are responding to the challenge through extensive employee training programs and through corporate contributions to private education. For its part, government, both federal and local, must enlarge support for education and worker training if U.S. industry is to possess the human resources to compete in world markets. We support a modest, targeted adjustment assistance program which would focus on retraining rather than unemployment compensation.

To recapitulate, policies to improve the competitiveness of U.S. industry are an essential response to foreign competition. We strongly recommend that the focus be on the infrastructure rather than on targeted assistance to specific industries. Government's role should be to create an environment in which the talents of the private sector can be focused to meet the competitive challenge.

Strengthening the Trading System

A significant obstacle to U.S. exports, and to foreign investments which generate exports, is the network of protectionist barriers imposed by foreign governments. In the next round of multilateral trade negotiations, the United States should press our trading partners to effect reductions in non-tariff barriers and other practices which stifle international trade. The support of Congress is essential if our negotiators are to have the authority and the flexibility needed to lead the world toward a more open international trading system.

Because the GATT enforcement mechanism seldom provides prompt and full relief from violations of the rules regarding unfair trade, and because the progress of GATT negotiations will be slow, the U.S Trade Representative and the Commerce Department should be prepared to step up bilateral negotiations with individual countries on unfair trade practices. We favor a tough U.S. government stance toward foreign competitors which violate internationally agreed trading rules but consistently fail to open their markets to American products. Last year Congress broadened the scope of Section 301 of the Trade Act of 1974, which empowers the President to negotiate or to take action to reduce or eliminate unfair barriers to U.S. exports by foreign nationals; that authority has recently been used by the Administration and we recommend further Section 301 actions be initiated as appropriate.

U.S. Export Policy

Another response to import competiton is to adopt policies to increase exports. Declines in industries adversely affected by imports can be offset by expansion of sales of American products and services abroad. On average, each billion dollars in exports creates 25,000 jobs.

In addition to reducing foreign barriers to U.S. exports, policies of our own government must be more supportive of exports. We favor strengthening the direct loan program of the Export-Import Bank as well as an aggressive mixed-credit program designed to force an international agreement to limit such practices; avoiding the use of economic sanctions and trade embargoes to implement--usually unsuccessfully--foreign policy objectives; reducing, to the maximum extent possible, delays and inefficiencies in the nation's export control program; and adopting Federal tax policies which do not impair the competitiveness of U.S. industry.

Growth Abroad

Along with the strong dollar, a principal reason for the recent surge in U.S. imports is the difference in growth rates between the U.S. and its trading partners.

The U.S. government should encourage all its trading partners interested in the preservation of an open international system to adopt responsible growth policies. This will have the effect of directly increasing U.S. exports and decreasing imports--particularly those "dumped" onto U.S. markets because of stagnant demand in other markets. Such policies would also make foreign countries more attractive to investment, thereby helping to reduce the exchange rate value of the dollar. Developing countries in particular, should adopt policies which will attract foreign capital and foster growth in order to be able to repay foreign debts and contribute to the expansion of world trade.

TRADE PROPOSALS IN CONGRESS

We believe the programs and policies outlined above constitute an effective response to America's import challenge. We turn now to a brief review of the principal import-restricting proposals before the Congress.

Anti-targeting Bills

A variety of proposals have been advanced to restrict imports of products which have benefited from foreign government industrial policies aimed at export expansion. Among the practices addressed by these bills are "targeting," broadly defined as foreign government assistance to export industries, and dual pricing of natural resources or products made from natural resources.

Bills aimed at "targeting" and similar practices reflect a growing concern by U.S. businesses that foreign government industrial policies are conferring special advantages on foreign competitors to the detriment of U.S. producers. In many cases the foreign government intervention to which U.S. producers object consists of subsidies, non-tariff barriers, dumping or other practices which violate the GATT or existing U.S. trade laws. In these cases, the appropriate U.S. government response should be more frequent and aggressive use of the trade remedy laws, and the filing and vigorous prosecution of more complaints in the GATT.

The fundamental difficulty with many of the proposals before Congress that address the problem of foreign government industrial policy is that they go beyond the international consensus as to what constitutes an unfair practice under internationally accepted trade rules. While sympathizing strongly with U.S. producers confronted with a variety of foreign government interventions which aid their export industries at our expense, we have strong reservations concerning unilateral legislation by the United States characterizing the industrial policies of our trading partners as unfair trade practices. We believe that enactment of a trade remedy law restricting imports of "targeted" products, for example, would involve the United States in futile and self-defeating conflicts with our trading partners, leading to retaliatory action abroad which would harm our exports. The fact is that many foreign governments play a more active role in directing their national economies than does the United States government. While recognizing that progress will be slow, we believe that the issue of industrial policies aimed at export promotion should be addressed either in the GATT, or in bilateral negotiations. An international consensus on the fairness or unfairness of such practices is needed; whereas U.S. laws unilaterally setting international standards would be inconsistent with the present GATT Subsidy Code. The Council has recommended that the GATT Subsidy Code be revised during the forthcoming multilateral trade negotiations to address new forms of subsidization and other unfair government intervention in trade. In the meantime, we recommend that our government and U.S. industry utilize existing laws and institutions to find relief from harmful foreign government export assistance.

Changes in Section 201 of the Trade Act

A second set of proposals in Congress call for changes in Section 201 of the Trade Act. The overall objectives of the proposals are 1) to expand the act so that more import-restrictive actions can be brought; 2) to make import relief more automatic and, 3) to enlarge the role of government in the formation of industry adjustment plans.

We recommend that these proposed changes not be adopted. Section 201 in its present form balances the interests of U.S. producers injured by import surges and the broad national interest in the consumption of fairly traded imports. Enlarging the coverage of Section 201 will produce more foreign retaliation against U.S. exports (permitted by the GATT) and will permit more U.S. industries which are uncompetitive to line up to seek shelter from import competition at a heavy price to non-protected industries, to consumers and to the U.S. economy.

With respect to proposals to enlarge the role of government in the formation of industry adjustment plans, either as a condition of import relief or as an instrument of industrial policy, we favor permitting injured or declining industries to work out their own destiny. Companies hard hit by injurious foreign competition may decide to retool, to retrench, or even to enter a whole new line of business. These decisions are best left to the marketplace, and not to the judgment of government planners.

Because the detrimental effects of import restrictions may outweigh the benefits of import relief, we endorse a number of the principal provisions of Senator Roth's bill (S.234), which would broaden the scope of the International Trade Commission's investigation into the impact of proposed import restrictions and would encourage the ITC and the President to recognize that industry difficulties, even when accompanied by rising import levels, can stem from factors unrelated to imports. These changes should lead to wiser administration of the statute.

Quota Proposals

A number of proposals have been introduced in Congress to protect individual sectors of our economy from imports. While import restrictions on particular products may have less adverse impact on the economy than a surcharge on all imports, or all imports from certain countries, the cumulative effect of restrictions on particular sectors is to close our borders to greater and greater volumes of imports, thereby setting the stage for similar actions by our trading partners and imposing greater burdens on non-protected industries by higher costs, misallocation of resources, and upward pressure on exchange rates. We urge the Congress to resist calls for additional quotas.

Substantial additional legislation to reduce imports is not the solution to America's trade problems. With few exceptions trade laws already on the books provide means of redress for domestic producers injured by import surges or by trading practices of foreign competitors recognized internationally as unfair. What is needed is more vigorous enforcement of these laws to eliminate unfair trade practices and provide U.S. industries with time to adapt to changing competitive conditions.

Import Surcharge

Still another proposed solution to import competition is the import surcharge. There are several bills in Congress which on either an across-the-board or a selective basis would impose a tax of as much as 25% on imports. It is, of course, far easier to tax the foreigner than to make the painful decisions involved in reducing the Federal budget deficit. But the easy course is not the sound course. An import surcharge would raise prices, jeopardize the economies of a number of developing nations, invite retaliation, and severely contract world trade. The Congressional

Budget Office has concluded that while some of the consequences of an import surcharge by the United States are unpredictable, there would be a significant risk of damage to the U.S. economy. Proposals for a discriminatory surcharge, e.g., against Japan alone or Japan plus several other countries based on statistical formulae, are particularly undesirable since such action would violate U.S. international commitments including U.S. treaty obligations.

Conclusion

Import competition presents a severe challenge to some sectors of American industry. But the solution does not lie in additional import restrictions. The challenge of import competition must be met ultimately by an economy characterized by rapid growth, in which new employment and investment opportunities open up to replace industrial sectors which are contracting, and resources flow from non-competitive sectors into sectors in which United States producers have a competitive edge. What is required to enhance the competitiveness of American industry is 1) a reduction in the exchange rate of the dollar, effected through control of the Federal budget deficit; 2) stronger action by our government to eliminate foreign and domestic barriers to trade; 3) policies to promote U.S. exports and the productivity of American industry; 4) strengthening the international trading system; and, 5) efforts by our trading partners to stimulate economic growth.

Coalition for
International
Trade
Equity

STATEMENT OF
RICHARD M. BRENNAN,
Executive Director

On Behalf of the
COALITION FOR INTERNATIONAL TRADE EQUITY

Before the
Senate Finance Committee
November 21, 1985

1625 EYE STREET, N.W. • SUITE 707 • WASHINGTON, D.C. • 20006 • (202) 822-0737

COALITION FOR
INTERNATIONAL
TRADE
EQUITY

CITE TESTIMONY BEFORE
SENATE FINANCE COMMITTEE
RE
"FAIR vs UNFAIR TRADE PRACTICES"

November 21, 1985

Introduction

Three graphics (Exhibits I-III attached) are included to demonstrate the current international economic reality -- namely, increased government intervention in international trade flows:

* The first map depicts the world according to the theory of free trade and comparative advantage.
* The second map, CITE believes, is a more accurate portrayal of international trading realities wherein various degrees of government intervention are depicted.
* The third graphic lists the specific market distorting practices of the major trading nations of the world.

CITE was formed in 1983 by a group of high tech companies concerned with the deterioration of the international trading system. In particular, CITE is concerned with international market distortions caused by the policies and practices of foreign governments, such as foreign industrial targeting.

Outstanding companies such as United Technologies, DuPont, Monsanto, Motorola, the Harris Corporation, Control Data, Olin International, Corning, Westinghouse and Timex are members of CITE.

Basis of US Law and the GATT

A basic axiom of US trade law is that international trade flows should be governed by natural comparative advantage as determined by market forces.

1625 EYE STREET, N.W. • SUITE 707 • WASHINGTON, D.C. • 20006 • (202) 822-0737

This is also one of the basic tenets of GATT. Stated another way, both US trade law and the GATT envisioned an international trading system based on an equivalence of competitive opportunity among enterprises and in which enterprises compete with one another; the actions of government should neither help nor hinder their respective competitive positions in international trade.

These are sound economic principles. Principles designed to serve all nations well over the longer term; which indeed they did for many years CITE companies are prepared to compete under these principles.

Is an International Trade Regimen Needed?

Yes, such a regimen is essential. All nations, no matter what their stage of development, benefit from having a system, a set of rules and guidelines.

Without some system of rules, the business environment for all participants would be uncertain; it would be almost impossible to plan for plant expansions, new product development, etc. The risk would be too great is such business plans could be scuttled by the arbitrary and capricious acts of a government.

Frame of Reference Needed

When discussing fair or unfair trade practices, a frame of reference appears essential. The above-mentioned basis of US law and the GATT, namely the equivalence of competitive opportunity concept, provides a once agreed to international standard.

It is a concept; exceptions to it were made at the outset by granting grandfather exceptions to certain practices (eg, other trade distorting practices are condoned when a nation is in Balance of Payments difficulties, etc).

Yet, the principles of the GATT and its conceptual precursor, the International Trade Organization, were well thought out and sound.

Our objective should be to reestablish an open international trading system based on these principles and concepts.

Current International Trade Realities

Today however, the international trading regimen has seriously deteriorated. "The trading rules set under the GATT are increasingly ignored or evaded." This was one of the conclusions of the Dunkel Commission in its report to the GATT Director General in March 1985.

This deterioration can be directly related to the willful acts of governments. Very few trade-distorting practices are caused by corporations -- dumping, patent infringement, and some isolated cases of antitrust violations. Thus, the flaunting of GATT rules is not a series of random coincidences; it represents the cummulative acts of governments to achieve their specific national goals.

Each nation-state has a sovereign right to establish whatever social and economic policies and programs it believes are necessary for the internal workings of its nation. However, when they deal in international commerce, they take on an additional responsibility; one, that to a certain extent, diminishes their sovereign right to act only in their own national interest.

It is this latter responsibility which is currently being ignored or evaded in international trade today. The ability of governments to devise unfair trade practices to protect or foster their industries appears boundless.

New Market Distorting Practices

One of the most elusive unfair trade practices to deal with under current US trade laws (and the GATT rules) is industrial targeting. The

International Trade Commission (ITC), in its extensive analysis of industrial targeting practices of other nations, developed the following useful definition:

> "Industrial targeting means coordinated government actions taken to direct productive resources to help domestic producers in selected industries become more competitive."

That industrial targeting practices exist has been well-documented. The most extensive and thorough analysis to date has been done by the ITC. Their three-volume study covered targeting practices in Japan, European Community Countries, Korea, Brazil, Mexico, Taiwan and Canada. The USTR and other US government agencies have also analyzed industrial targeting practices of other nations.

Industrial targeting exists; it is oftentimes both protectionist and predatory; it represents a significant combination of trade practices or government actions which result in international market distortions. It is "unfair" in that it confers a "government-created" comparative advantage upon its domestic producers in order to increase their competitiveness in international markets at the expense of their foreign competitors.

The practice of industrial targeting has evolved over several decades. In retrospect, the techniques used by Japan to enhance the competitiveness of its steel industry, starting in the 1950s, was a form of targeting -- we simply didn't call it that.

What is new about targeting?

* It adds the element of goal-oriented governmental combination of actions.

  In years past, governments subsidized or protected industries in a selective manner. Now, they combine a series of actions to foster the competitiveness of their domestic industries.

- It is being adopted and practiced by an increasing number of nations, particularly the NICs and the LDCs.
- Because of the rapid dissemination of technology (and gains in technology itself -- eg, transportation, communications), it is having a direct effect on international markets quickly.
- It was not anticipated by GATT or US law -- both are inadequate to deal with it.

  Some practices are legal under GATT, others are not; some are actionable under US law, some are not.

  However, the combination of practices constitutes an unfair, market distorting trade practice as the result of a "government-created" comparative advantage. The resulting commercial advantage is far greater that it would be absent such government actions. (This has been documented by both the ITC and USTR studies of targeting.)

  (A list compiled from the ITC studies of product sectors targeted by various nations is attached -- Exhibit IV.)

What is Fair or Unfair? A Case Study

Whether or not something is fiar or unfair is seemingly determined by where you sit. Our purpose here is to give the view of a US business organization and the dilemma it faces.

The basic frame of reference of most American manufacturers is the equivalence of competitive opportunity principle; in essence, our businesses are willing to compete with other enterprises as long as neither competitor receives special benefits from its respective government.

The dilemma facing the American manufacturer can best be illustrated by looking at the Japanese semiconductor industry. It is a useful illustration because it has been analyzed so closely and extensively.

The Japanese semiconductor case is also a good example of the structural change that has taken place in the international economic system over the last decade or two. This is thr structural change mentioned above, namely, the increasing involvements of governments in the business process.

The Trade Act of 1984 called for an analysis of foreign industrial targeting practices. One part of the analysis was to look at the international effects of targeting and the second aspect was to evaluate the effectiveness of US trade laws in responding to targeting.

The targeting practices of the Japanese semiconductor industry was one of the sectors studied. The analysis was conducted by Quick, Finan and Associates.

The Quick, Finan analysis evaluated the following targeting practices used by Japan to foster their semiconductor industry:

* Home Market Protection -- in the form of restricting US investment in Japan (although the US was the technological leader at the time), quantitative restrictions on imports and discriminatory government procurement practices.

* Tax Benefits -- Particularly in the early years of product development, a broad range of tax incentives were provided to the semiconductor industry. These tax benefits were phased-out or curtailed in later years as the product approached the commercialization stage.

* Antitrust -- The Japanese modified their antitrust laws to permit rationalization of R&D projects as well as production and marketing.

* Scientific, Technology and Financial Assistance -- The government of Japan provided a wide range of supports to its semiconductor producers.

All of these Japanese targeting practices were operating in parallel. Quick, Finan estimated that these combined Japanese targeting practices (excluding past restrictions on US investment in Japan) resulted in a loss of US market share by US firms ranging from between 9 and 24 market share points.

Quick, Finan estimated separately that the Japanese restrictions on US investment in the 1960s and 1970s cut the US participation in the Japanese market by about half -- it could have reached 40 percent rather than 17 percent.

Thus, the detailed analysis of the Japanese targeting or semiconductors demonstrates the effectiveness of specific market distorting effects of targeting. The Japanese semiconductor industry has definitely received long-term competitive benefits because of the actions of its government.

However, the second phase of the analysis, the effectiveness of current US trade laws to respond to targeting practices, epitomizes the frustration of American manufacturers -- in essence, this USTR analysis of US laws indicates there is little, if any, recourse or relief from targeting practices under current US law.

The USTR analysis reviews each targeting practice mentioned above against our three major trade laws -- antidumping, countervailing duty law, and Section 301. Summarized below are their findings:

* Most of these targeting practices are not related to dumping.
* Many of the subsidy practices associated with the Japanese semiconductor targeting are severely reduced or phased-out at the time of their major export drive and thus, there is nother to countervail against.
* Section 301 is considered to be of little value for a variety of

reasons. Either the practice does not lend itself to 301 criteria (for example, anti-competitive behavior) or the practice is considered GATT-legal (for example, certain home market protection practices or discriminatory government procurement practices that are carried out by government agencies not covered by the Government Procurement Code).

Note: Under Section 301, "unreasonable" is defined as "any act, policy or practice, while not necessarily in violation of or inconsistent with the international legal rights of the United States, is otherwise deemed to be unfair and inequitable." This would appears to cover acts that are GATT-legal; thus, the above interpretation of the USTR in this connection appears to go totally against the language in the statute.

Summary

The Japanese semiconductor case is illustrative of the ability of governments to cause major international market distortions. It simply highlights the structural change that has taken place in the international economic system during the post-War period. Japanese targeting practices are the visible tip of the iceberg; the other nine-tenths of market distorting practices of other governments are there -- they are just not quite as visible or obvious -- yet.

The Japanese targeting of semiconductors provides two rather sobering and disquieting lessons. The first is how effective governments can be in causing market distortions.

The second lesson is how quickly we in the US tend to forget the genesis of these government-created comparative advantages. The current plight of the American semiconductor industry is very grim -- plant closings, massive layoffs, companies going out of the semiconductor business, etc.

For some rather inexplicable reason, American commentators prefer to focus on what is wrong with us -- poor management, lack of American competitiveness, low productivity, poor labor-management relations, etc, etc. Certainly, American manufacturers are not perfect; but we should not lose sight of the fact that the Japanese government set out in the early 1970s to employ protectionist and predatory practices to dominate the semiconductor industry. If such irresponsible international commercial practices are permitted to continue without any response from the American government, such practices will lead to the undermining of our present private enterprise market system. (We seemed to have suffered similar memory losses in other industries such as steel, machine tools, shipbuilding.)

Over the last decades, a major structural change has taken place in the international economic system. During the period, the direct (and indirect) involvement of governments in the business process has increased dramatically. This is truce among the advanced nations of the Western world, the newly industrialized countries, and the developing countries.

This major change is significant because of the direct impact it has had on the way international business is now conducted. During the last decade, there has been a proliferation of trade distorting practices -- Orderly Marketing Agreements, Voluntary Export Restraints, the Multi-Fibre Agreement, exceptions to Most-Favored-Nation treatment, closed markets, subsidization, local content requirements, targeted industry programs, import quota systems, government procurement practices, etc. This litany of trade distorting practices can be applied to virtually every nation in the world; the US is no exception. Many of these practices are outside the surveillance or jurisdiction of any international framework or agreement such as the GATT.

Trading tensions in the world are increasing and escalating in importance. CITE believes there is a need within the US to understand more fully some of the root causes of these changes in the world trading system and to recognize that other nations are not going to adopt our economic system. CITE believes US laws and the international trade regimen, such as the GATT, must be modified in such a way that permits these different economic systems to co-exist and accommodate (rather than confront) one another in order to keep international trade as open as possible.

CITE is a coalition of high tech companies from a broad spectrum of industry who share a deep concern about the international trade environment. Based on its analyses and experiences in the international trade arena, CITE has concluded that that flow of international trade is governed less and less by market forces based on free competition and comparative advantage of one company versus another company.

The US reluctance to enforce its international trading rights cannot go on without causing additional serious erosion of the American manufacturing base. Such an erosion does not bode well for the continuance of the American role as the economic and political leader of the free world.

Because of the rapidity of change which is taking place in international markets, there is an urgent need for the US to take on its leadership role by enactment and enforcement of stronger US trade laws.

We cannot continue as a nation to be a "paper tiger" -- if we do so, other nations will continue to be complacent in joining us to reestablish an open and fair international trading system -- why should they "give up a good thing." The US must demonstrate its resolve to reestablish such a system by strong actions which demonstrate our complete intolerance of market distorting trade practices.

Recommendation

CITE's key recommendation to achieve these goals is embodied in proposed changes to Section 301 of the 1974 Trade Act by defining foreign industrial targeting as an unfair trade practice, reducing Presidential discretion, and making an American response mandatory in all injurious targeting cases.

CITE supports the proposed changes to Section 301 contained in S. 1356 and S. 1476.

Comment

It is our understanding that the current proposal would address the problem of targeting in both Section 201 and 301. We believe this approach would place an unnecessary burden and expense on American petitioners.

In Section 301, an unfair trade statute, only some targeting practices are defined as unreasonable.

We agree with the concept of identifying targeting practices under Section 301 and to give the President authority to pursue these market distorting practices. We also agree with the two new concepts of targeting added in the definition of unreasonable -- namely, infant industry protection and sanctioning of anti-competitive behavior.

However, there are other key targeting practices which we believe should be added.

Further, one of the major shortcomings of Section 301 has been the reluctance (almost refusal) of Presidents to exercise their authority under Section 301, usually for foreign policy reasons, not economic reasons. The fact that a President has used Section 301 only once in its history to retaliate (just this month) is a clear indication of the need for the Congress to build in procedures which require action. This is particularly necessary in the case of foreign industrial targeting when a foreign nations uses a combination of practices to provide their domestic industries a "government-created" comparative advantage over American businesses.

In Section 201, a fair trade statute, the proposal would authorize the US ITC to find "threat of serious injury" by imports because of the existence of foreign industrial targeting practices.

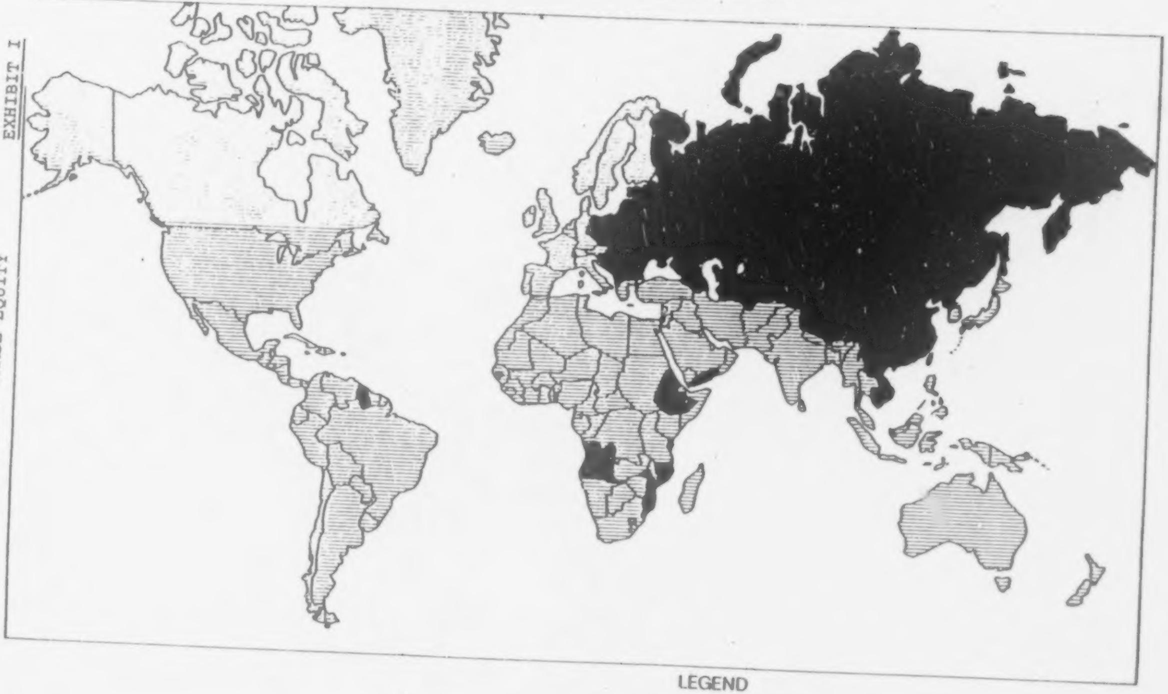
The proposed amendment to Section 201 will not be effective for several reasons:

* First, imports will have to be the principal cause of threat of injury to the industry to get relief. This means that targeting must be the number one threat to the industry before action will be taken.
* Second, to the best of our knowledge, the ITC has never made an affirmative determination in a Section 201 case based solely on a finding of threat of injury.
* Third, even if the ITC were to find targeting to be a threat of injury, it is unlikely, under the proposal, that the President would take action. Presidents have only granted import relief in 25 percent of the cases filed.
* Fourth, the US has advocated that so-called "safeguards" be applied on a Most-Favored-Nation (MFN) basis in order to conform to GATT objections. Section 201 is an MFN-type statute seeking relief from all imports. Foreign industrial targeting is practiced by individual nations.

Conventional Economic Theory View of the World

COALITION FOR INTERNATIONAL TRADE EQUITY

EXHIBIT I



LEGEND

▤ Free Trade Economies

■ Non-Market Economies

EXHIBIT II

COALITION FOR INTERNATIONAL TRADE EQUITY

Current International Trade Realities

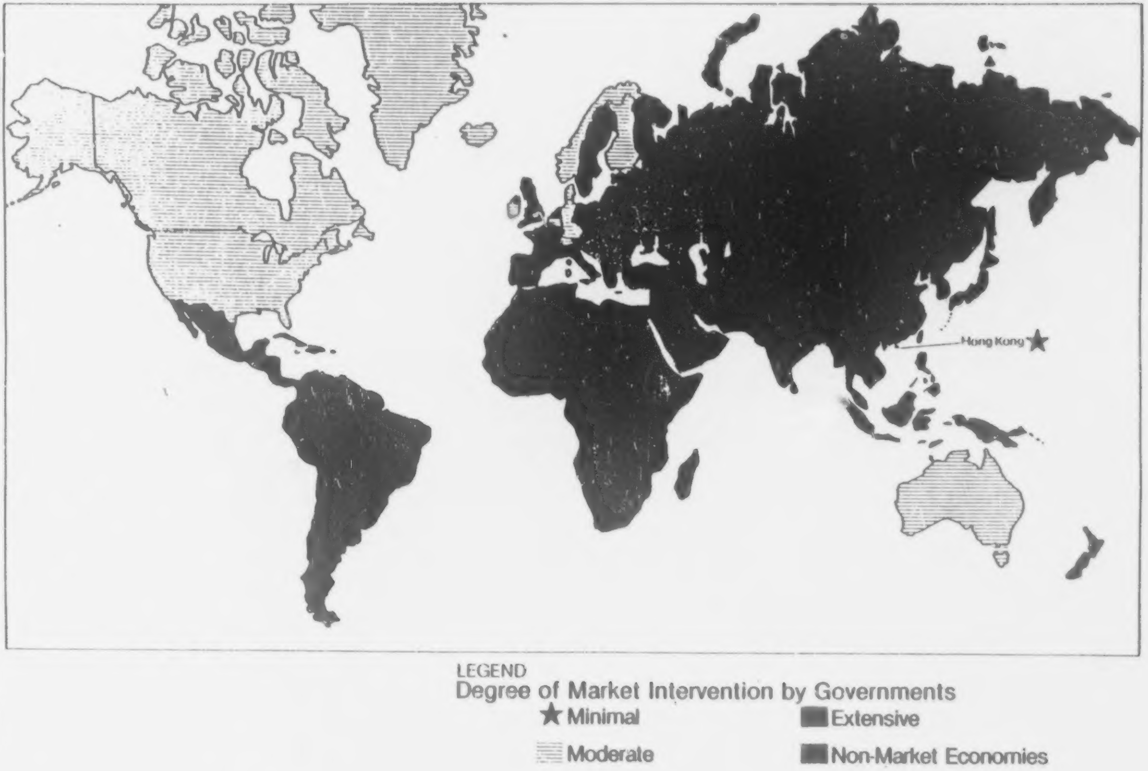

Hong Kong ★
LEGEND
Degree of Market Intervention by Governments
★ Minimal
▤ Moderate
■ Extensive
■ Non-Market Economies

EXHIBIT III

COALITION FOR INTERNATIONAL TRADE EQUITY

GOVERNMENT CREATED MARKET DISTORTIONS IN SELECTED COUNTRIES AS REPORTED IN RECENT STUDIES OF PAST AND PRESENT USES OF SUCH PRACTICES

GOVERNMENT CREATED MARKET DISTORTIONS	HONG KONG	US	EUROPEAN COMMUNITY	WEST GERMANY	UNITED KINGDOM	FRANCE	CANADA	JAPAN	SOUTH KOREA	BRAZIL	MEXICO	SINGAPORE	TAIWAN
Home Market Protection:													
Tariffs		★	★	★	★	★	★	★	★	★	★		★
Quotas		★	★	★	★	★	★	★	★		★		★
Discriminatory Government Procurement		★			★	★	★	★	★	★	★		★
Other Non-Tariff Barriers			★	★	★	★	★	★	★	★	★	★	★
Tax Policies:													
Special Depreciation Rules				★	★	★	★	★	★	★	★	★	★
Exemption for Export Earnings								★	★	★		★	★
Tax Deferral for Export Earnings		★						★		★			★
Antitrust Exemptions:													
Mergers			★	★		★		★	★				
Price Fixing Cartels			★	★				★					
Rationalization Cartels			★	★		★		★	★				★
Export Cartels				★				★					
Joint Research & Development		★				★		★					
Restrictions Against Competition			★					★					
Science & Technology Assistance:													
Support for Research & Development			★	★	★	★	★	★	★	★		★	★
Control Over Technology Imports							★	★	★	★			★
Assistance in Acquiring Foreign Technology				★		★	★		★	★			★
Training				★	★	★	★	★	★	★		★	★
Financial Assistance:													
Loans at Preferential Terms			★	★	★	★		★	★	★	★	★	★
Loan Guarantees			★	★	★			★	★	★	★		
Export Financing		★		★	★	★	★	★	★	★	★		★
Preferential Access to Investment Funds					★			★	★	★	★		
Preferential Access to Foreign Exchange			★					★	★	★	★		
Grants			★	★	★	★	★	★	★	★	★	★	
Foreign Investment Controls:													
Restrictions (prohibition) on Investment in Certain Sectors							★	★	★	★	★		★
Export Performance Standards									★	★	★		★
Other Performance Standards (including Technology Sharing)							★	★	★	★	★	★	★
Government Ownership:													
Nationalized Industries			★		★	★	★			★	★		★
Firms in Selected Industries State-Owned			★	★	★	★	★	★	★	★	★	★	★

COALITION FOR INTERNATIONAL TRADE EQUITY EXHIBIT IV

INTERNATIONAL TRADE COMMISSION (ITC) REPORTS: INDUSTRIES TARGETED BY FOREIGN GOVERNMENTS

JAPAN -- October 1983

- Aircraft
- Aluminum
- Automobiles
- Computers
- Iron & Steel
- Machine Tools
- Semiconductors
- Telecommunications

EUROPEAN COMMUNITY -- April 1984

- EC Policies:
  - Coal
  - Computers/Peripherals
  - Machine Tools
  - Steel
  - Textiles
- France:
  - Aircraft/Aerospace
  - Apparel
  - Autos/Trucks
  - Telecommunications
  - Electronics
  - Heavy Electrical Equipment
  - Machine Tools
  - Semiconductors
  - Textiles
- United Kingdom:
  - Aircraft/Aerospace
  - Autos
  - Computers/Peripherals
  - Heavy Electrical Equipment
  - Machine Tools
  - Semiconductors
  - Telecommunications
- West Germany:
  - Aircraft/Aerospace
  - Autos
  - Information Technologies
  - Machine Tools
  - Semiconductors
- Italy:
  - Apparel
  - Autos

BRAZIL, CANADA, KOREA, MEXICO, TAIWAN -- January 1985

- Brazil:
  - Aerospace
  - Autos
  - Computers
  - Heavy Electrical Equipment
  - Footwear
  - Pharmaceuticals
  - Semiconductors
  - Shipbuilding
  - Steel
  - Telecommunications
  - Textiles/Apparel
- Canada:
  - Aerospace
  - Autos
  - Petroleum/Gas
  - Telecommunications
- Korea:
  - Autos
  - Computers
  - Heavy Electrical Equipment
  - Machine Tools
  - Pharmaceuticals
  - Shipbuilding
  - Steel
  - Textiles/Apparel
- Mexico:
  - Autos
  - Computers
  - Petroleum/Gas
  - Pharmaceuticals
  - Steel
- Taiwan:
  - Autos
  - Electronics
  - Machine Tools
  - Petroleum/Gas
  - Pharmaceuticals
  - Shipbuilding
  - Steel
  - Textiles/Apparel

STATEMENT OF ROBERT L. McNEILL, EXECUTIVE VICE CHAIRMAN
EMERGENCY COMMITTEE FOR AMERICAN TRADE
BEFORE THE COMMITTEE ON FINANCE OVERSIGHT HEARINGS ON UNITED STATES TRADE POLICY

November 21, 1985

I am pleased to be here to express some views on the the general question of U.S. policy toward "fair" and "unfair" trading practices.

While the determinant of what is fair and unfair is often in the eye of the beholder, there are some objective measurements found in international law and practice - principally in the GATT. The GATT deems certain "subsidies", "dumping," and the nullification or impairment of negotiated trade benefits to be unfair trade practices against which injured parties can retaliate. U.S. statutes reflecting these GATT rules are found in our antidumping and countervailing duty statutes and in Section 301 of the Trade Act of 1974.

The GATT also has rules allowing parties to impose import restrictions against products that are traded internationally under "fair" trade practices. Article XIX of the GATT authorizes the imposition of import restrictions to relieve serious injury caused to domestic industries by fairly traded competitive imports and GATT Articles XII and XXI respectively authorize import restrictions to safeguard national balance of payments positions and the national security. U.S. statutes reflecting these GATT rules are found in Sections 201-203 of the Trade Act of 1974, Section 122 of the same act, and Section 232 of the Trade Expansion Act of 1962 in the case of the national security safeguard.

There are thus three "unfair" trade practices that are explicitly recognized in the GATT and reflected in U.S. "unfair" trade statutes. Similarly, there are three "fair" trade practices recognized in the GATT pursuant to which import barriers can be imposed and that also are reflected in U.S. "fair" trade statutes.

In addition to the above six instances, the United States utilizes one other major "unfair" trade practice statute and that is Section 337 of the Tariff Act of 1930. The United States also utilizes one other safeguarding statute that can pertain to fairly traded items and that is the Trading with the Enemy Act, which was used in 1971 by President Nixon when he declared a national economic emergency and imposed a ten percent import surcharge.

From the above summary, I think it can be fairly stated that United States defensive statutes toward both "fair" and "unfair" trade practices are generally in accord with international law and practice. We do, however, have a number of domestic economic policies that our trading partners view as either illegal or questionable under international laws and practices. Several are mentioned later.

Beyond the "fair" and "unfair" trade practices noted above, there is no international agreement as to fairness in trade practice. We hear every day about "level playing fields" and about the purity of U.S. practice when compared with the practices of others. We hear that it is unfair for one country to have higher tariffs than another and that there can be no fair trade in the world until there are no differentials in wage rates. Government assists to production are deemed to be unfair - unless the assist is for the benefit of the speakers. It is not remarkable that the litany of complaints are universal. These are heard in every country about every other country.

"How should 'fair' and 'unfair' trade be distinguished?" is one of the questions asked by the Finance Committee of the witnesses at this hearing. I would submit that the appropriate answer is by international agreement. Unilateral answers can well invoke undesired responses. Should, for example, the United States pioneer new ground by unilaterally determining that certain foreign subsidies are subject to U.S. countervailing duties despite long-standing international agreement that they are not, then this would subject U.S. exports to foreign retaliation. A similar result would follow the imposition of other U.S. trade barriers that did not accord with our international agreements and obligations such as legislative import quotas on textile and apparel imports. There is no suggestion intended here that problems should not be dealt with. They should but in the context of developing sound international solutions that will protect and further the interests of all concerned. Thus the real need for a new round of international trade negotiations where a variety of trade concerns can be handled.

We in ECAT strongly support the President and Ambassador Yeutter in their determination and their actions to vigorously enforce our trade statutes and to seek improved access for U.S. exports and investments abroad. We particularly applaud the steps being taken by Secretary Baker and others to strengthen the value of the yen and other foreign currencies against the dollar. The overvalued dollar is the single most important factor affecting the international competitiveness of American business. Hopefully, the governments of

Japan and West Germany in particular will implement their September 22, 1985, agreements at the G5 meeting to stimulate their respective economies. If they do, that will be a great assist for U.S. exports and the U.S. economy.

International negotiations on unfair trade practices when undertaken will be contentious and arduous. There is a number of countries who are unwilling to negotiate on their practices and who are unwilling to expand the international rules to cover trade in services, to provide surety for the sanctity of intellectual property rights or to expand on current unfair trade agreements in such areas as government subsidies. Most of these countries are developing countries with whom our trade was booming prior to the international debt crisis. They firmly believe that their economic status fully justifies maintenance of a number of "unfair" and restrictive practices that they believe will assist their economic development.

The task of developing international understandings on both fair and unfair trade practices is thus an exceedingly difficult one. A good start was made in the Tokyo Round of multilateral trade negotiations in negotiating international codes on subsidies, dumping, government procurement and standards. There are thus building blocks in place that can be both improved and added to.

Ambassador Yeutter expressed concern and frustration to this Committee last week at the apparent efforts of a small number of GATT countries to frustrate the beginning of a new round of trade negotiations in Geneva. He expressed an unwillingness to allow these countries to torpedo such negotiations and suggested that like-minded countries should consider working together on a new round. While this would be regrettable since it would be a significant move away from the current multilateral trading system, it might prove necessary if we are to progress in our effort to open world markets.

A direction for such negotiations exists in the principle underlying the Tokyo Round codes and that is that the obligations and benefits are applicable to the signatories of the codes and not to those who do not choose to become a party to them. While a conditional form of most-favored-nation treatment, it is open to all and thus offers the possibility of universal application.

If there are to be major and comprehensive trade negotiations and if the issue of fairness is to be a part of them, then all participants are going to have their trade-related practices examined by their negotiating partners. While the United States will have a lengthy catalogue of complaints about foreign unfair trade practices, so will others submit complaints about some of ours. Obvious ones that have been cited in the past include U.S. import quotas on agricultural products, agricultural subsidies and subsidies for exports of agricultural and other products. Government expenditures for research and development, for irrigation and inland waterways and for the development and transmission of hydroelectrical power also have been raised as "unfair" economic practices in the United States.

I would like to conclude with a rather radical but I believe sensible proposal for consideration by this committee and by others with responsibilities for international trade. It is a purely personal suggestion that has not been considered by the members of ECAT. The proposal is that we abolish unfairness as a basic criterion for restricting imports and adopt as the only valid basis for restricting imports whether they are causing serious injury to a domestic industry. As has already been learned through our international trading experience, the concept of unfairness is especially difficult to define in objective terms. Just like Justice Potter Stewart's famous dictum about obscenity, any given observer may think he knows unfair trade when he sees it, but he can't adequately define it. The concept of unfair trade has thus become a highly contentious one among trading countries. One country's notion of unfair trade may be quite different from another's, and the term has thereby become a provocation for dispute rather than a basis for sound policy.

A major reason for my suggestion is that the concept of unfair trade attempts to judge an act by its inherent character rather than by its consequences. The concept is directed to whether an act is fair or unfair and totally disregards what is the effect of the act, whatever its character. The basic consideration should be whether imports are causing serious injury to a domestic industry! Under such unfair trade statutes as the countervailing and dumping duty laws, it first has to be determined whether an unfair subsidy or a margin of dumping exists before the question of serious injury is examined. While the "unfairness" investigation is ongoing, the serious injury may well be done.

Were my proposal to be given serious legislative consideration, I would recommend that the new standard be based on the concepts in Sections 201-203 of current trade law, recognizing that serious thought would be required as to the new threshold definitions of injury as well as to the discretion that would be available to the President.

I have not addressed the issue of whether existing trade practice statutes are adequate nor have I commented on the question of the adequacy of import relief provisions. Should there be any questions on these issues, I would be pleased to respond.

Thank you for the opportunity to be here today.

STATEMENT OF THE
COALITION TO PROMOTE AMERICA'S TRADE
BEFORE THE
COMMITTEE ON FINANCE
UNITED STATES SENATE

HEARINGS
ON UNITED STATES TRADE POLICY

Of Counsel:

Charlene Barshefsky
Steptoe & Johnson
1330 Connecticut Ave., N.W.
Washington, D.C. 20036

November 27, 1985

STATEMENT OF THE COALITION TO PROMOTE AMERICA'S TRADE

The Coalition to Promote America's Trade is an _ad hoc_ organization of American petrochemical and agricultural companies that was formed in early 1984 to support fair and free trade and to oppose passage of so-called "natural resource subsidy" trade legislation.

Within the broad context of the trade issues that this Committee is presently considering, the Coalition would like to focus on the natural resource question, and wishes to emphasize two major points.1/ First, the concerns that underlie the "natural resource subsidy" proposals, when properly viewed, are not problems of unfair pricing practices by foreign governments. They are, therefore, not properly addressed through the countervailing duty law. Rather, the question of U.S. producer access to low-cost foreign natural resources and the underlying issue of reciprocity, which are at the heart of the natural resource debate, can already be effectively addressed under section 301 of the Trade Act of 1974. Second, in attempting to cast the natural resource issue as one involving unfair pricing and subsidies, the natural resource proposals incorporate serious conceptual flaws, so that their

---

1/ In this statement, the Coalition bases its position on the arguments presented in more detail in the recently published article, Barshefsky, Diamond & Ellis, "Foreign Government Regulation of Natural Resources: Problems and Remedies Under United States Trade Laws," 21 _Stanford J. Int'l L._ 29 (1985).

implementation would give rise to grave economic and trade-related repercussions.

- Arguments used to justify the proposals are based on a model of private business behavior that is unrealistic, and on a view of the legitimate scope of government activity that is contrary to the United States' own regulatory conduct.
- Enactment of such a proposal would have serious anticompetitive implications and serious trade repercussions.
- The proposals would be unadministrable and foreign compliance virtually impossible.

The Coalition would like to address each of these points.

I. AMENDMENT OF THE COUNTERVAILING DUTY LAW TO ADDRESS THE NATURAL RESOURCE QUESTION IS Ill-ADVISED

We would first like to outline our specific concerns about the legislative proposals that would amend the countervailing duty law. A few basic points deserve mention. The thrust of the natural resource proposals is to declare as countervailable the sale by foreign governments of government-regulated natural resources to local purchasers at prices below what is termed a "fair market price" and below the price at which the resource is sold to United States purchasers for export to the United States. The amount of the countervailable subsidy would be the difference between the foreign country's domestic price and the "fair market price" of the resource.

The subsidy would be applied against a product made from the resource in the foreign country and exported to the United States.

In determining fair market value, the two major proposals, S. 1292 and section 502 of S. 1356, authorize consideration of various factors. Such factors include the natural resource's export price, the prices at which it is generally available in world markets, whether foreign markets are available to the exporting nation to sell the natural resource, and the competitive market-clearing price at which the resource can be sold in those foreign markets.

It is clear from the description of the proposals that they do not and are not intended to attack the provision by governments of natural resources at prices below the fully allocated cost of production. Sales below cost can be effectively addressed under the current U.S. antidumping law. Rather, the proposals would radically expand the countervailing duty law to treat as countervailable subsidies a country's natural cost advantages. They would do so by redefining the concept of unfairness to include situations in which it is determined that government sales -- while made at prices not only above fully allocated cost, but above fully allocated cost plus profit -- were not profitable enough. This radical expansion of the countervailing duty law suffers from the following defects:

- The legislation expects governments to behave in a manner different from many private enterprises in making pricing decisions.

- The proposals conflict with the internationally accepted view of the scope of legitimate government activity.
- The proposals condemn government activities in the regulation of a nation's natural resources similar to those that have routinely been undertaken by the United States.
- The proposals have serious anticompetitive consequences in that they act to reinforce and strengthen the market power of cartels.
- The proposals would invite retaliation against United States exports by our trading partners, or the enactment of "mirror" legislation.
- The proposals are impossible to embody in predictable, enforceable legislation.

Allow us briefly to elaborate on these points.

A. The Proposals Expect Governments to Behave in a Manner Different From Many Private Enterprises in Making Pricing Decisions

The proposed legislation constitutes a radical departure from U.S. unfair trade laws and accepted principles of international trade. This legislation is not designed to condemn sales below fully allocated cost, nor even sales made at a handsome profit; rather, it attacks any sale made at less than the immediate short-term profit maximizing price. Until the present proposals, the trade laws have never been interpreted to compel enterprises -- private or government-regulated -- to operate at a specified level of profit, let alone engage in short-term rather than long-term profit maximization. Yet this is precisely what the natural resource proposals would do.

This ill-advised expansion of the countervailing duty law is justified by proponents of natural resource legislation as a way to restrain the behavior of foreign governments by limiting them to actions taken by private businesses. The assumption made is that only one market strategy is available to a private company -- that of maximizing short-term profits. In fact, this assumption is often wrong. In forcing governments to pursue short-term profit maximizing strategies as the only way in which downstream products can "fairly" be sold on world markets, the proposals expect governments to behave in a manner that private enterprises often do not satisfy.

In contrast to the simplistic view of private business behavior embodied by the natural resource proposals -- quick sales at the highest price -- diverse market conditions and different attitudes toward risk and long-term growth may lead companies to pursue radically different marketing strategies. Companies may choose to undersell the market in order to trigger an immediate growth in sales. They may lower prices to selected buyers, or seek long-term supply commitments, all in furtherance of longer-term growth. Or a company that sees a potentially lucrative new market for its products may lower its prices to the infant companies that are creating that market to help improve their chances of success. These varied strategies are often adopted by U.S. companies; indeed, they are required by the diversity of the market place. To penalize foreign governments for pursuing similar long-term strategies simply imposes limits on them which U.S. companies have never had to meet. Similarly, to define as an "unfair practice" the failure to reap maximum short-term profits on sales made abroad sets an extremely dangerous precedent which could be used to attack as "unfair" our own U.S. exports.

B. The Proposals Are Contrary to the International Consensus as to What Constitutes a Subsidy and Conflict with U.S. Development of its Own Natural Resources

Not only are the natural resource proposals based on an unrealistic view of private business conduct, but they also ignore the internationally accepted nature of the government activities involved here. Governments are quite properly motivated by broad general welfare considerations that may result in behavior different from that of a private company. One means by which governments have attempted to improve their nations' general welfare is by developing their natural resources. The impact of such development on their societies may be dramatic.

The fact that a government acts to promote the general welfare of its citizens does not necessarily immunize it from the imposition of countervailing duties under current U.S. law and GATT principles. But the international community has agreed -- and the United States has firmly supported the proposition -- that such actions are exempt if the benefit provided is generally available to all citizens. Both the GATT Subsidies Code and United States law recognize that to be countervailable government benefits must be sector specific in nature. Generally available benefits -- such as U.S. control of oil prices in the 1970's -- have been staunchly defended by the U.S. as non-countervailable. Indeed, the European Community has accepted this argument, and in 1980, it agreed not to initiate a countervailing duty investigation of U.S. petroleum-based products such as synthetic fibers, because the low U.S. regulated price of the natural resource was made generally available throughout the U.S. economy.

Generally available benefits may take myriad forms. For example, a government may distribute part of the income generated from sales of a natural resource directly to its citizens, or use such funds to provide roads, schools, hospitals or food. Alternatively, the government may provide a resource which it owns directly to its citizens at low prices or, by regulation, require that the resource be sold at low prices. The United States has frequently engaged in this type of resource distribution, for example, in selling power generated by federal dams at very low rates, in selling cheap water from government river control projects in the West, or in regulating the prices at which oil and natural gas may be sold. Few examples of greater magnitude exist than the land grant programs sponsored by the United States government during the nineteenth century.

By abandoning the requirement under GATT and our current law that countervailable domestic subsidies be sector-specific, the proposals run directly counter to the long-term interests of the United States. Since a vast array of "generally available" government economic programs can be said to benefit a country's producers, no clear line can be drawn between government action that is countervailable and government action that is not. Using the examples cited above, if generally available inexpensive natural gas is a subsidy, why not water from government irrigation projects benefiting agricultural products? Cheap hydroelectric power produced by government dams? Investment tax benefits to corporations? At the extreme, as noted by the Court of International Trade in a recent decision construing the sector-specific requirement, even public highways and bridges could be considered countervailable government benefits to their users, and "almost every import entering the stream of American commerce [could] be countervailed."[2/]

That such a result is not intended with respect to natural resource development was made abundantly clear in the recent Congressional debates on the extension of the contracts that would provide power generated at the Hoover Dam at prices far below market rates. Numerous defenders of the proposal -- of both parties and in both Houses of Congress -- argued that the contracts would allow the government to charge enough to recover costs and perhaps earn some profit (though certainly not the highest possible profit), and more fundamentally, that throughout United States history, the role of government in the

---

[2/] Carlisle Tire & Rubber Co. v. United States, 564 F. Supp. 834, 838 (C.I.T. 1983).

development of this nation's resources has never been that of a profit-maximizing entity.

The bill reauthorizing below-market pricing of hydroelectric power from the Hoover Dam passed both Houses of Congress by substantial margins. The numerous statements made in support of that legislation apply with equal force to the provision of natural resources by foreign governments to their people:

- "The primary purpose of the Federal hydropower program is not to maximize revenue at taxpayer's expense but to sell power at the lowest possible rates . . . and recover the Government's investment and operating expenses." (Rep. Jerry Patterson, D-Cal.)
- "[T]he whole concept of public power was one in which we said Government was not going to make a profit on the power." (Rep. Allan Swift, D-Wash.)
- "There is no subsidy involved. What is involved here is that the whole philosophy of Federal power production is that [sic] get cost recovery." (Rep. Mo Udall, D-Ariz.)
- "The Federal Government is not in the power business to make a profit -- but to stimulate private development of energy resources. The purpose of the Federal power program has never been to maximize revenue but to sell power from public projects at the lowest possible rates that will recover the Government's investment and pay all operating expenses. The projects should pay their own way -- and Hoover does." (Rep. Howard Berman, D-Calif.)
- "There is no subsidy inherent in the concept of tying the price of power to its cost of production. This is the way 98 percent of all power in America is priced." (Sen. Chic Hecht, R-Nev.)

- "[W]e ought to be pricing the power on the basis of what it costs to produce it." (Sen. James McClure, R-Idaho)

- The Federal Government is not in the business to make a profit. . . . [I]n each of [its] investments we have done it at the lowest possible price in order to give to the people of this country . . . an opportunity to better themselves. . . .

  [The] policy which has been held in this country, in my view, for virtually all of its 200-year history . . . [is] to build this infrastructure for what it costs and to regain those costs, but not to make a profit beyond that . . . . I think it has been a good policy, it is a good policy, and will continue to be a good policy." (Sen. Daniel Evans, R-Wash.)

- "There is no need for the United States to make a profit from federal hydropower resources. . . .

  Clearly the arguments for market pricing are specious. It is against the public interest." (Sen. Barry Goldwater, R-Ariz.)

- "While some will argue that we should not be selling Federal power at below-market rates, the primary purpose of the Federal power program is not to maximize the Government's revenues but to sell power from public projects at the lowest possible rates to consumers that will recover the Government's investment and pay the operating expenses." (Sen. Dennis DeConcini, D-Ariz.)

In short, the regulation and development of a nation's natural resources have long been recognized by the United States as falling within the legitimate scope of government activities, as to which countervailing duties do not apply. No compelling argument has been advanced to alter this view.

C. The Proposals Have Serious Anticompetitive Consequences and Will Strengthen the Market Power of Cartels

The proposals provide an exception to countervailability in the event the foreign nation permits United States producer access to the low-priced resource (again revealing the importance of the access issue to the natural resource proposals). But where such access is denied -- whether for political or other reasons -- that nation can comply with the proposal only if it raises its internal price of the resource to so-called "world market" levels. In already cartelized markets for certain natural resources, serious economic repercussions would arise from such a pricing measure.

As a matter of economic policy, the lowering of world prices of natural resources more accurately to reflect costs of production should be sought. Instead, however, the natural resource proposals would directly counter this type of positive economic activity. In utilizing "fair market value" to determine the extent to which the internal price of the resource is subsidized, these proposals essentially mandate the use of cartel prices, whenever a cartel exists, as the benchmark against which the subsidy is to be calculated. Undercutting the cartel price is penalized; reinforcing the cartel price is accomplished. This latter point is particularly disturbing when one considers that U.S. law would effectively extend a cartel's price discipline to countries not currently a member of the cartel. A more irrational result -- the legitimizing of inflated world market prices for natural resources -- could hardly be imagined.

The natural resource proposals would not merely lead to a lessening of competition in the natural resource itself, but also would have an obvious and direct adverse impact on American businesses and consumers. Using natural gas as an example, compliance with the proposals would force the prices of imported energy-intensive products -- such as ammonia -- to rise. The result could well be higher food prices for American consumers. So, too, the prices of imported cement to U.S. industries would rise, further escalating already high costs of construction. While these are but two of innumerable examples, it is clear that the natural resource subsidy proposals have serious commercial implications both at the level of the natural resource and at the level of the downstream product.

D. The Proposals Will Adversely Affect Foreign and Domestic Trade

Enactment of the natural resource proposals could significantly impede or disrupt United States trade. Disruption would occur not only because of the potential retaliatory actions that other countries might take in response to such legislation, but also because of the effect that these proposals would have on existing purchaser/seller relationships.

Retaliation against United States exports would be likely. As noted earlier, the United States countervailing duty law provides for a general availability test in determining whether a particular domestic subsidy is countervailable. Article 11(3) of the GATT Subsidies Code, enumerating specific examples of possible "domestic subsidies," specifies that such subsidies are those "granted with the aim of giving an advantage to certain enterprises," and are "normally granted either regionally or by sector." These references form the basis for the explicit requirement in United States law that only domestic benefits "provided to a specific enterprise or industry, or group of enterprises or industries" are countervailable.

Last year, the Administration, after close study, concluded that in light of the sector specificity rule, the natural resource proposals considered in the 98th Congress constituted "a drastic and unilateral departure from the internationally accepted definition of a countervailable subsidy," in violation of GATT, and that enactment of such a provision "would subject the United States to a GATT challenge, which we would almost certainly lose. The result could be GATT authorization to retaliate against U.S. exports." The Administration reiterated its position earlier this year in hearings on one of the natural resource subsidy proposals (H.R. 2451, introduced by Congressman Gibbons) before the Trade Subcommittee of the House Committee on Ways and Means -- a proposal identical to S. 1292 and section 502 of S. 1356. Likely targets for retaliation would be our own major exports, such as agricultural and textile products. Even if the natural resource proposals were to survive a GATT challenge, it would be a pyrrhic victory, for foreign governments would then have every encouragement to enact their own "mirror" legislation.

Key United States exports would become less competitive on the world market. The adverse impact of the natural resource proposals on United States exports extends far beyond GATT retaliation or the enactment of mirror legislation. Many United States industries use basic petrochemical and other natural resource-derived products imported from other nations to make more advanced products, which are then exported from the United States. American agricultural interests, petrochemical industries, and the forest products industry, to name just a few, all utilize natural resource-based products to produce downstream goods for export. If the prices of the basic products are driven up by substantial duties, the prices of the exports of the finished products will also rise, severely undermining or destroying their competitiveness in world markets. The marketplace would thus "retaliate" against United States exports, even if our trading partners did not.

The proposals would seriously jeopardize United States relations with developing countries. Finally, the natural resource proposals would hit hardest at United States trading partners in the developing world, where regulation of natural resources is frequently an essential part of long-term economic and social development. Indeed, the GATT recognizes the difficult economic situation of the developing nations, by allowing them greater commercial latitude without the threat of retaliation. And the United States for decades has repeatedly urged those nations to rely on the development of their natural resources to diversify their productive capacity, improve their financial position, and enhance the welfare of their people. Enactment of the proposed legislation would clearly undermine the substantial progress made by these countries.

United States exporting industries would also be substantial losers if duties were imposed on products from the developing world. These countries are major purchasers of United States exports: for example, some forty percent of total United States agricultural sales now go to developing countries, and these countries are the key growth market for future United States agricultural sales. It is simply not in the interest of the United States to jeopardize substantial long-term trading relationships with these countries, as would be the case were this legislation enacted.

E. The Proposals Are Virtually Unadministrable and Compliance Impossible

In addition to the anticompetitive and adverse trade-related consequences of the natural resource subsidy legislation, compliance with and predictable administration of the proposals are virtually impossible.

- The proposals send a "damned if you do, damned if you don't" signal to foreign governments and producers. Under present United States law, the foreign exporting industry would run afoul of the antidumping statute if the natural resource in question was exported at a price lower than the domestic price of that resource. At the same time, however, under the natural resource proposals, such producers would also be committing an "unfair" practice if the export price of the resource were greater than the price charged in the domestic market. Indeed, such a result would obtain even if there were no exports of the resource in question; under such circumstances, a "fair market value" analysis would govern. Compliance with United States trade laws would thus be virtually impossible for affected foreign exporters, however the natural resource was priced.

The proposals are virtually impossible to embody in predictable, enforceable legislation. The proposals employ terms which are impermissibly vague or impossible to quantify. For example, they specify certain factors to be used in determining "fair market value," including "market clearing price," and "generally available" prices in "world markets." Although understandable concepts, such terms are not amenable to precise calculation. Moreover, no guidance is provided as to their relative weight, or the manner in which they are to be balanced against the domestic price of the resource. Indeed, as the International Trade Commission stated in its section 332(b) investigation of natural resource pricing, "[f]or a nation that has no current viable natural gas export market, the domestic price cannot be compared to the world natural gas price."[3/] The very vagueness inherent in the concepts employed in these proposals underscores the fact that no foreign country, however it priced its resources, could be assured that its practices would comply with United States law. This unpredictability is itself a barrier to trade.

The same indefiniteness also renders unworkable reliance on the "export price," which is one factor that the proposals would consider in determining fair market value. Just as myriad internal prices may exist for a resource, so too, a broad spectrum of export prices may be available for comparison purposes. No guidance is provided, however, for adjusting those prices to reflect vastly different terms and conditions of sale.

F. An Injury Test Does Not Mitigate the Proposals' Serious Flaws

The proposals provide an injury test, according to which injury must be demonstrated by the petitioning United States industry before countervailing duties may be imposed, even though for all other purposes under the countervailing duty law the foreign nation may not be entitled to an injury test. While the provision of an injury test may mitigate a proposal's impact in specific cases, it does not address and thus cannot mitigate the underlying conceptual problems that

---

[3/] U.S. International Trade Commission, Potential Effects of Foreign Governments' Policies of Pricing Natural Resources (Final Report on Investigation No. 332-202 Under Section 332(b) of the Tariff Act of 1930) at xv (May 1985).

plague the proposals. Nor can the presence of an injury test resolve the practical problems with the proposals, such as their anticompetitive effects, their negative market impact on American consumers and export business, and their impossibility of administration and compliance.

II. THE PROPOSALS ARE UNNECESSARY, BECAUSE PRESENT U.S. TRADE LAW PROVIDES A REMEDY FOR THE PRACTICES ALLEGED

Enactment of a natural resource proposal is unnecessary in light of the fact that United States trade law -- specifically section 301 of the Trade Act of 1974 -- already provides a remedy for the practices complained of by proponents of the legislation. As is evident from the natural resource debate, the proposals are intended not merely to remedy alleged foreign pricing improprieties, but also to gain access for United States producers to foreign natural resources at low internal prices. The proposals demonstrate the importance of access by defining a "natural resource subsidy" to exist only where the price of the resource "is not freely available to United States producers for purchase of the input product for export to the United States." An effective natural resource remedy is thus one through which access may be achieved while, at the same time, providing for the imposition of duties or other forms of trade relief in the event access is denied.

The access and pricing issues involved in the natural resource debate are concerns that can be specifically addressed under section 301 of the Trade Act of 1974. This is not merely the view of the Coalition. It is also a view expressed by some of the chief proponents of natural resource legislation. This was made clear in numerous meetings of an industry *ad hoc* working group formed to study the natural resource issue. Industry proponents and opponents of natural resource legislation which participated in these working group sessions included domestic ammonia producers, an ammonia importer, and companies participating in petrochemical ventures abroad. The trade experts of these companies exhaustively studied the issue of natural resource subsidies, including an analysis of current U.S. trade laws and the applicability of those laws to the natural resource issue. The working group unanimously concluded that "Section 301 provides a potentially effective remedy to questions of natural resource pricing and access."

Some members of the working group nonetheless believed that legislation should still be sought because section 301 relief is discretionary. However, it is clear from examination of the record in section 301 proceedings that some sixty percent of section 301 cases have been successfully resolved by USTR. It is also clear that section 301 is broad enough in scope to address adequately problems of both natural resource pricing and access. Given these facts, there is no justification whatever to change fundamentally the U.S. countervailing duty law to address the natural resource issue. This is especially true in light of the grave economic and trade-related repercussions of such a change in that law.

Section 301 authorizes the President to respond, inter alia, to "unfair" or "unreasonable" trade practices of foreign governments that "burden or restrict United States commerce." Upon the filing of a petition and initiation of a proceeding, the Office of the U.S. Trade Representative may consult or negotiate with the offending country in order to achieve a bilateral resolution of the alleged violation. This is the most typical way in which section 301 actions have been successfully resolved. To the extent such negotiations fail, the President ultimately may retaliate by imposing duties or other forms of import relief, or by taking other action which adversely affects merchandise exported to the United States from the foreign nation. The President's action may be directed against all countries on a nondiscriminatory basis, or solely against the offending nation.

Unlike the countervailing duty (and antidumping) laws, the range of unfair or unreasonable practices covered by section 301 is far more flexibly defined. The conduct that is at the core of the natural resource subsidy dispute -- the denial of equivalent access for United States producers to foreign resources, and the question of reciprocity -- falls squarely within the scope of the statutory language. That a remedy is available under section 301 is especially clear when one examines the amendments to that law that were enacted just last October -- amendments that make explicit the ability of the United States to attack the type of practices at issue here. For example, the law now defines the term "commerce" to include "foreign direct investment by United States persons with implication for trade in goods and services." And the definition of the term "unreasonable" has been expanded to include acts or practices that deny "market opportunities" or "opportunities for the establishment of an enterprise" by United States parties in the foreign nation. These provisions of section 301 thus have as their aim an opening of foreign investment and access opportunities for United States producers -- precisely the concerns addressed by the natural resource proposals.

In addition to its statutory language, section 301 relief is far superior to that available under the countervailing duty (or antidumping) laws. Section 301 relief can be long-term. The ultimate forms of relief available under the statute -- bilateral resolution, duties, quotas, tariff rate quotas, retaliatory action, and the like -- are far more varied than those available under any other unfair trade law. The practices of individual countries may be addressed both individually and flexibly. And the time frame for resolution of such actions in the case of non-signatories to the GATT (e.g., Mexico, Saudi Arabia, the U.S.S.R.) is, by statute, approximately one year -- substantially less than the time frame involved in countervailing duty proceedings, given the numerous opportunities for judicial review of those determinations.

It is true that in the event bilateral consultations fail to produce adequate results, the ultimate relief available under section 301 is discretionary with the President. But, in fact, some sixty percent of all actions under section 301 have been successfully resolved through bilateral consultations between USTR and the offending nation, or, on rare occasions, the imposition of other forms of relief. By contrast, in 1984 only 48 percent of antidumping and countervailing duty cases were successfully resolved. Included in the section 301 figures are actions sucessfully prosecuted against such countries as Canada on certain tax practices, Argentina on leather hides, China on certain restrictive import practices, Taiwan on rice -- countries and products or practices as to which diplomatic and political sensitivities are acute. Given the obvious applicability of section 301 to the pricing and access issues raised by proponents of the legislation, and the track record in other complex and controversial section 301 proceedings, a change of such dramatic proportions as would be involved here to the current countervailing duty law is simply unjustifiable.

LET'S REBUILD, AMERICA
IN THE 80's

Statement of the Chamber of Commerce of the United States

ON: THE GROWING CLAMOR FOR PROTECTIONISM

TO: SUBCOMMITTEE ON ECONOMIC STABILIZATION OF THE
HOUSE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

BY: FRANK L. MORSANI

DATE: JUNE 26, 1985

The Chamber's mission is to advance human progress through an economic,
political and social system based on individual freedom,
incentive, initiative, opportunity and responsibility.

The Chamber of Commerce of the United States is the world's largest federation of companies and associations and is the principal spokesman for the American business community. It represents more than 180,000 companies plus several thousand other organizations such as local/state chambers of commerce and trade/professional associations.

More than 90 percent of the Chamber's members are small business firms with fewer than 100 employees, 53 percent with fewer than 10 employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business--manufacturing, retailing, services, construction, wholesaling, and finance--numbers more than 14,000 members. Yet no one group constitutes as much as 29 percent of the total membership. Further, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the 53 American Chambers of Commerce Abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross section of its members serving on committees, subcommittees and task forces. Currently, some 1,800 business people participate in this process.

STATEMENT
on
THE GROWING CLAMOR FOR PROTECTIONISM
before the
SUBCOMMITTEE ON ECONOMIC STABILIZATION
of the
HOUSE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
for the
CHAMBER OF COMMERCE OF THE UNITED STATES
by
Frank L. Morsani
June 26, 1985

Mr. Chairman, members of the Subcommittee, I am Frank L. Morsani, Chairman of the Board, Chamber of Commerce of the United States of America. I am also President of Precision Enterprises in Tampa, Florida.

Introduction

We congratulate the Chairman and members of this Subcommittee for convening this hearing. We are well aware of the frustration that you feel concerning increased U.S. trade deficits and unfair foreign trade practices. The growing clamor for protectionism, as you have so aptly characterized it, continues to rise with every passing month, despite passage of major trade legislation last fall. Left unchecked, protectionist tensions threaten to undermine and possibly destroy the multilateral trading system that has served to promote world trade and economic growth since World War II.

A number of factors have contributed to the rise of protectionism. Uneven economic growth worldwide, high unemployment in some areas, volatile exchange rates, and government market intervention, as well as unavoidable structural changes in the world economy, have all fueled dissatisfaction with the current system. But by closing our markets to foreign competition, we would bring about results all of us should fear. If those who call for restrictions, here and abroad, retain the offensive and obtain the market-closing policies they seek, we will risk a worldwide collapse of trade that could be worse than the Great Depression of the 1930's. If this should occur, the overall health of our relationships with other nations stands to deteriorate. All segments of the American public, including the Administration and Congress, as well as business, labor and academia, must recognize this and begin to grapple with this challenge.

The domestic U.S. economy is increasingly integrated with the world economy. The percentage of the U.S. economy accounted for by exports and imports has doubled over the last twenty years. It is now over 20% of our Gross National Product. Greater interdependence is obvious in trade, finance, investment and technology.

In short, our trade interests are inseparable from not only our domestic interests but also our diplomatic, strategic and military interests abroad. Disruption in any one of these areas threatens stability and progress in all of them.

Numerous examples abound: for example, President Reagan's announcement of his intention to embargo trade with Nicaragua not only raised new questions about the renewed use of trade as a weapon but also brought into focus a new disagreement between us and our allies on U.S.-Central American policy, a major foreign policy issue.

Against the backdrop of continuing record U.S. budget deficits, the U.S. and its allies find themselves unable to agree on the purpose of international monetary talks or even to set a date for multilateral trade negotiations.

And, as we all know, the 1974 OPEC oil embargo and resultant price increases and dislocations made the average American realize, perhaps for the first time, that we can not ignore the world economy. Even today, petroleum imports account for 25% of our trade deficit. We are as dependent on "them" as "they" are on "us."

As we meet the trade challenge, we must not forget that.

America's Challenge

U.S. international economic performance is at a crossroads. The $123 billion merchandise trade deficit for 1984 has brought into clear focus a potentially dangerous situation that has been developing for some time. Since World War II, with the advent of U.S. world trade leadership, we have viewed ourselves as second to none. Left largely unscathed at home by the ravages of WWII, America's leadership in world affairs seemed unchallengeable. We assumed leadership in drafting the multilateral trade order known as the General Agreement on Tariffs and Trade (GATT) which took effect in 1948. The seven major rounds of trade negotiations under GATT auspices are principally responsible for the widespread and substantial reductions in tariffs worldwide.

The United States has also played a leading role in global finance and development affairs. In 1944, at Bretton Woods, New Hampshire, a U.S.-led conference of forty-four nations agreed to establish two international institutions for the purpose of promoting a stable, peacetime global economic environment. The International Bank for Reconstruction and Development (also known as the World Bank) was established for the purpose of making long-term reconstruction and development loans. With over 140 member nations, it is the world's largest single aid donor, as well as the largest borrower in the international bond market. Its development mission, made possible by the Marshall Plan, has reached around the world. The International Monetary Fund (IMF) is charged with the provision of short-term assistance (loans) to countries with balance-of-payments problems. Through its efforts to promote international monetary cooperation and stability, the IMF seeks to facilitate the expansion of trade and, in turn, increase world employment and economic growth.

Both institutions, while not without problems, clearly represent the best intentions and leadership abilities of the United States. As leaders, in business and in government, we must to continue this traditon. We must ensure that the substance of our leadership truly reflects the aspirations of humanity--freedom, opportunity, peace, and prosperity.

However, our leadership is under challenge as never before. The continuing evolution of the world economy and the dislocation it is causing are leading many Americans to question the very foundations of the world economy and the trading system which we have helped to shape. The advantages we enjoyed relative to other nations when the GATT system was formed have all but disappeared as other nations have developed. In many cases, rules which were intended to help them when they needed help now provide them with significant advantages. More often than in many years, Americans are viewing the world trade and financial system as a threat to their well-being, rather than an opportunity. They see the U.S. trade deficit reaching record levels. They see the shift in emphasis from manufacturing to services and high-technology but have doubts about its future. They see developing countries attempting to cope with their indebtedness but view the IMF as an agent of big-bank bailouts.

The observation that the U.S. is rapidly becoming the world's largest debtor nation frightens many Americans. Massive international capital flows in the direction of the U.S. have helped to finance the U.S. budget deficit and other credit needs. It is important to note that while annual inflows of foreign savings have remained relatively stable since 1981, net U.S. capital outflows have fallen significantly. In other words, a major factor underlying overall capital inflows into the U.S. is the decline in U.S. capital leaving the U.S., and not a major increase in foreign savings in the U.S. Nonetheless, there is concern among many that someday, under as yet unforeseeable circumstances, overall capital flows may reverse direction, out of the U.S., greatly increasing the cost and difficulty of financing U.S. credit and investment needs.

In short, the world trade and financial system suffers a crisis in confidence where confidence may matter most--here in the United States. And we have yet to formulate a policy to restore this confidence.

Protectionist Trends

These concerns are not new. We have seen them before. The Smoot-Hawley tariff of 1930 started as a relief measure for agricultural products. Yet, it became the most protectionist legislation in American history. Numerous amendments were adopted, and tariffs were raised to record levels. Much of the world retaliated, and all of us paid with a longer and deeper Great Depression.

International financial institutions are not free from controversy and criticism either. Two years ago, Congress narrowly averted serious problems when it agreed to pass IMF quota increase legislation. That legislation substantially increased confidence in the IMF to address what many regarded as the worst international financial crisis since the 1930's. Passage of this legislation was not without rough sailing, however. Many Americans expressed understandable but misplaced fears that the quota increase would be abused to cover past bank management failings. In response to these fears, new constraints to check such abuses were adopted.

We can cite numerous examples of departures from free trade. Nations around the world engage in elaborate trade-distorting practices. Japan's use of countless, complex non-tariff barriers is legendary, accounting for an estimated $10 billion of their trade surplus with the United States. The Europeans' use of agricultural export subsidies poses a major problem for the farm sector and, as much as anything else, undermines our efforts to achieve harmonious trade relations with the European Economic Community. The less developed countries and the newly industrialized countries find themselves forced to subsidize their manufactured and raw material exports in order to obtain foreign exchange and service their debt. At the same time, their domestic political situation makes it difficult for them to provide market access anything like our own.

In the United States, the last recession served to increase resentment of foreign imports enjoying substantial market share while Americans were being laid off. The increasing importance of the service and "high-tech" sectors relative to manufacturing and stronger foreign competition in both areas have highlighted the importance of adjustment, as well as the clamor for protectionism that results.

And perhaps most important of all, the wild fluctuations in exchange rates, including a substantial appreciation of the dollar in the last five years against major currencies, have posed important challenges for U.S. industry. Many U.S. exporters and import-competing companies correctly blame the strong dollar for a major decline in their ability to compete. In addition, the instability of exchange rates, regardless of the actual ratio, introduces new uncertainty and risk into business decision making. This brings higher costs, inflationary pressure and greater market concentration.

Trade Policy from the 1930's to the Present

Beginning with the enactment of the 1934 Trade Agreements Act, the U.S. government has commendably taken a number of steps which recognized the folly of protectionism and worked to open the trading system. Pursuant to the spirit and letter of GATT, Presidential flexibility to reduce trade barriers and negotiate trade agreements under GATT was enhanced. Under the Trade Act of 1974, less developed countries (LDCs) were granted duty-free access to the U.S. market under the terms of the Generalized System of Preferences. The Tokyo Round of trade negotiations achieved agreement on several non-tariff issues. Congressional passage of the 1979

Trade Agreements Act served to implement these agreements. At the same time, Congress did what it could to make sure that unfair practices, such as dumping and subsidies, remained subject to sanctions. A process of relief from injurious imports, as well as from a potentially wide range of unfair foreign trade practices, was included in Sections 201 and 301 of the 1974 Trade Act.

In 1984, the last significant trade legislation, the Trade and Tariff Act, was enacted. The managers of this legislation, in particular including my own Congressman, Sam Gibbons, should be commended for their efforts to maintain and strengthen the trading system. Renewal of GSP is vitally important to the maintenance of mutually beneficial trade between the U.S. and less developed countries. Equally important, the so-called reciprocity provisions in Title III provide important new tools for the President to negotiate for greater U.S. trade and investment access to foreign markets. However, the 1984 Act is at least as notable for what is not in it as for what is in it.

Current Problems

While the 1984 Act represents a tentative victory for open trade forces, the strong continuing dissatisfaction with U.S. trade performance has led to the introduction of numerous trade proposals in the 99th Congress. Some of these proposals closely resemble provisions seriously considered but set aside by the 98th Congress as it debated the 1984 Act.

I do not doubt that Congress will soon place trade issues at the top of its legislative agenda. Anyone who even glances at a newspaper or watches TV can see that trade is a major issue. The consequences of Congressional action will be important and may be far-reaching. Therefore, it is imperative that all who are involved in trade policy distinguish fact from fiction when identifying issues and considering responses.

For example, Americans increasingly single out Japan as the principal, if not the sole, villain against whom we must prevail in the world market. Japan's $37 billion trade surplus with the United States, it is said, is principally the result of countless trade-distorting practices developed through government-industry collusion. Regardless of their actual impact, these practices are unbefitting a highly developed nation. Unless Japan quickly eliminates these practices, they may find access to the U.S market denied or sharply restricted.

There is no question that Japan's markets are effectively closed to many foreign enterprises. We recognize that culture and tradition (e.g., "keiretsu") play an important role in determining strong Japanese preferences for domestically produced goods. However, Japan must take meaningful action now to open up its markets to a degree comparable to the access we provide to U.S. markets. This includes sales of goods and sevices, as well as investment. Failure to take these steps now will only worsen the political climate between our countries. Left unattended, the deterioration of relations between our countries will soon reach the point of no return. Once that happens, both sides will likely enter a downward spiral of retaliation, recrimination and stagnation in which everyone loses.

We Share Responsiblity

Nonetheless, we should not overstate the significance of Japanese trade barriers or their relationship to the trade deficit, irritating though these may be. The fact of the matter is that the major portion of the so-called "Japan problem" is made right here in the U.S.A. If Japan were to eliminate all of its trade distorting practices overnight, optimists estimate that our bilateral trade deficit would be reduced by about $10 billion--less than one-third of the total. The unpleasant truth is that, regardless of questionable Japanese trade practices, the U.S. business community needs to improve its performance in many ways. Let me make some observations about the relative state of Japanese and U.S. industry:

-- Japanese manufacturing productivity has risen almost three times faster than that of America since 1970.

-- The Japanese savings rate is much higher than the U.S. rate. The excess of Japanese savings over domestic investment is "exported" to other countries, keeping the yen's value down without deliberate currency manipulation. The result is greater price-competitiveness of Japanese exports.

-- The Japanese capital stock has been growing over twice as fast as the American since 1970. As a result, Japanese equipment is much newer than American equipment.

-- The large increase in the Japanese share of the world market for cars, trucks and ships reflects both cost and quality advantages.

These are important differences which must be narrowed in America. We cannot rightfully expect Japan, or any other nation, not to compete effectively in the marketplace, even though we may insist that they play by the rules. The choice here is largely ours.

It is also worth observing that, on a per capita basis, Japan is not the worst trade offender, if merely sustaining a trade surplus can be called an offense. While Japan, with a population of 120 million, had a $37 billion trade surplus with the U.S. last year, Canada, with only 25 million people, had a $20.6 billion surplus. In other words, on a per capita basis, Canada's merchandise trade surplus with the U.S. was three times as large as Japan's in 1984. And yet, while we talk about punishing Japan with new trade restrictions, we are contemplating free trade areas with Canada. This is simply not fair.

Some believe that the trade deficit or the strong dollar is "deindustrializing" America. The data do not support this. It is true that some firms and industries, such as basic steel and mill products, have declined over the last several years. But other sectors, such as communications equipment and electronic components, have grown impressively. Since 1980, growth in overall U.S. industrial production, at 12 percent, topped that of each of the seven major industrial countries except Japan. Indeed, production in Italy and France, with their weak currencies, actually fell since 1980 while it increased only 2 percent in Britain.

This is not to say that some otherwise highly competitive firms have not suffered over the past few years as a consequence of the sharp appreciation of the dollar. They most certainly have. What we are saying is that in the aggregate, thanks in large part to domestic, growth-oriented tax, budget and regulatory policies, U.S. industrial production has substantially improved, both in absolute terms and relative to most of our major trading partners.

The same point can be made about overall U.S. economic performance. The evidence is clear that, among the seven major industrial countries, those with low-tax/low-spend policies are out performing high-tax/high-spend countries in both employment and output. The solution to what is described as the dollar problem and foreign stagnation lies in a greater convergence of U.S. and foreign economic policies. Specifically, this means foreign emulation of demonstrably successful U.S. economic policies--tax and spending cuts, deregulation and disciplined, non-inflationary monetary policy. In addition, Congress must weigh carefully the ramifications of proposed major changes in the Internal Revenue Code as they affect worldwide savings and investment. Tax simplification proposals, such as "Treasury II," represent the most significant revisions of the tax code in at least a generation. We must remember, again, that our actions in this regard will have repercussions extending well beyond our borders. We urge Congress to keep this in mind as it pursues its deliberations.

While fiscal and monetary policies are important determinants of U.S. international competitiveness, those calling for protection believe that closing off or restricting world trade provides jobs and stimulates growth by insulating industries from an inherently "unfair" and unforgiving market. But history clearly shows us that "insulation" leads to industrial stagnation, wasted resources, fewer jobs and lower living standards. Sluggish growth and increased unemployment in the U.S. and around the world are the inevitable results.

Recommendations

The best trade policy for promoting growth and jobs is one that recognizes our growing interdependence as an opportunity. Such a policy will favor expansion and liberalization of the trading system, not restriction. We must maintain efforts to lower trade barriers abroad and resist pressures to close our own markets. The prospect of severe damage to the trading system resulting from protectionist initiatives makes it even more timely for the Chamber to reaffirm its support for actions that result in trade liberalization worldwide. Our recommendations include the following:

- o Effective enforcement of U.S. laws in defense of our trade rights under international rules can help ameliorate growing pressure for counterproductive trade-restrictive measures.

- o The Chamber reaffirms its opposition to protectionist measures, such as import surcharges, quotas, domestic content laws and restrictive trade laws in conflict with our international obligations.

- o The Chamber supports Presidential use of tools provided in Title III of the Trade and Tariff Act of 1984 in order to obtain increased market access abroad. Restrictive trade barriers in other nations deny U.S. exporters, investors and service firms a fair opportunity to compete. It is difficult for the United States to retain its status as a relatively open market accessible to other nations when equivalent access is not enjoyed by U.S. companies overseas. This is particularly pertinent in the case of advanced developing countries that enjoy duty-free access to the U.S. market provided under GSP but continue to maintain trade-distorting practices and restrictions in their own countries. GSP is important to world trade and it should be continued. But it must not be abused.

- The Chamber also supports new and dedicated multilateral efforts to reduce barriers and to restore and improve discipline and stability in the world trading system. Priorities should include (but not necessarily be limited to) strengthening the disciplines of the international trading system; further reductions of tariff and non-tariff barriers; improvement of the performance of GATT machinery and secretariat; adaptation to the growing concerns surrounding services, investment and intellectual property rights; the linkage of trade and monetary matters; further integration of LDCs into the world trading system; maximizing public support for improvement of present trade rules and institutions; and Congressional renewal of Presidential negotiating authority.

Congress has before it several restrictive proposals aimed specifically at Japan. The prospect of a serious conflict between the world's two most important trading nations deeply concerns the Chamber. We believe that sustained growth and development of commerce in the Pacific basin represent one of humanity's best hopes for the next century. This region, with its rapidly growing, dynamic market-oriented economies, gives every indication that it will assume world economic leadership for the forseeable future. A healthy, vibrant U.S.-Japan relationship in trade and, indeed, in all matters is critical to the success of the region and the world economy.

We recognize that numerous unresolved differences exist between the United States and Japan. Trying to resolve these differences may on occasion cause the U.S. government to take unilateral action which will prod our Japanese friends to be more forthcoming in their efforts to reach agreement.

However, Congress and the Administration must carefully define the problems to be solved, as well as the manner in which they are to be solved. The Chamber's positions in this regard are the following:

- The Chamber opposes legislation that mandates the President to take retaliatory action against any country. The Chief Executive's flexibility as embodied in existing law must be retained. Denial of such flexibility will make targeting responses to specific developments far more difficult, thereby reducing the chances of obtaining the market access or other outcomes we seek.

- The Chamber does believe that on a case-by-case basis the Administration should exert greater leverage, using existing mechanisms of multilateral and bilateral negotiations and agreements. These include Article XXIII of the GATT, the "nullification or impairment" clause. If these efforts fail, then the U.S. should exercise its rights under domestic and international trade laws and consider major changes in existing domestic and international arrangements governing trade.

Let me take this opportunity to tell you about an emerging trade issue on which the U.S. Chamber is taking a leadership role: access to the rapidly growing worldwide telecommunications market. The opportunity to compete fully and fairly in foreign markets is a fundamental objective of the American business community. Nowhere is this more important than in the emerging worldwide high technology markets, particularly those associated with what some call the global information economy, which spans a range of products and services connected with the generating, processing and distribution of information. Computer hardware and software, micro-electronics, and telecommunications technologies are all vital to the operation of the global information economy. Furthermore, rapid technological change is increasingly blurring the demarcation among these segments.

Unfortunately, we must recognize that a key to this global information economy, the national telecommunications markets, remains among the most highly regulated areas of business activity. Because these telecommunications networks must serve as the central transportation system for the global information economy, progress towards greater competitive opportunities in telecommunications is critical to the future growth of trade in high technology products and services. Recognizing this fact, the U.S. Chamber is working closely with members of Congress to help shape constructive legislation that would encourage the negotiation of greater access for U.S. firms to worldwide telecommunications markets. In the absence of such negotiation, the U.S. business community may well be denied the opportunity to compete in this dynamic part of the world economy.

I think it is important to note at this point that the current administration has demonstrated a clear willingness to exercise leverage, including the use of substantial import restrictive measures, in order to secure cooperation from our trading partners on the question of trade liberalization. For example, the Administration took a dramatic step in this fashion last fall when it banned most European steel pipe and tube imports until the end of 1984 in reaction to perceived non-compliance with steel pipe and tube import agreements.

This administration has taken some restrictive measures of a substantial nature even when it is less clear that the purpose of such measures is to promote negotiation or clarification of an agreement. In April of 1983, President Reagan approved a 45 percent increase in duties on imported motorcycles. The President has taken a number of actions to reduce textile and apparel imports, the most recent major action being the U.S. Customs Service's promulgation of the revised "country-of-origin" rules as they related to "substantial transformation" of textile and apparel products in different countries.

The steel quota system currently in effect is even stricter than the Multifiber Arrangement (MFA) on textile and apparel imports. Unlike the MFA, the steel quota system sets a worldwide ceiling for imports. It includes Europe, not just Japan and developing countries. Imports are prohibited from growing more rapidly than the domestic market. Perhaps most significantly, the steel industry can dismantle the system by filing unfair trade practice cases.

The point here is that, if and when Congress begins to debate trade legislation, it should recognize that this administration has clearly been willing and able to use its existing authority to impose trade restrictions in order to cushion a variety of industries from foreign competition. In our view, the record simply does not support the contention that the Administration has been unwilling to use the tools currently at its disposal to remedy injurious or unfair trade practices.

Chamber International Programs

The U.S. Chamber is uniquely situated to work toward increased market access worldwide. Through an extensive network of 53 affiliated American Chambers of Commerce abroad, representing some 60,000 firms and individuals, American business diplomats are engaged in breaking down barriers to U.S. trade, investment and services every day. AmCham presidents, committee chairmen and other American residents abroad meet face-to-face with host country government and business policy makers. Perhaps the most notable current example of such involvement is that of the president of the American Chamber of Commerce in Japan. He and his AmCham colleagues have been at the forefront in advising every U.S. government negotiating team to visit Tokyo over the last year. He has gained such credibility that he was appointed as one of the two foreign business representatives on the new Advisory Committee to the Japanese Ministerial Committee charged with implementing the pledges contained in Prime Minister Nakasone's April 9 statement.

In addition, the Chamber sponsors 14 bilateral business councils bringing some 700 U.S. corporate executives together with their counterparts from key trading areas around the world. For example, just a few weeks ago, together with our India-U.S. Business Council, we held an off-the-record discussion for 40 senior corporate executives with Prime Minister Gandhi of India. This meeting, along with other similar sessions we have held with some 20 heads of state or government in the last 18 months, provides an opportunity to press for improved business conditions for American exporters, importers, investors and service firms. Mr. Chairman, I think we have had a few successes. Some important countries are opening up slowly. But we have a long way to go before we achieve a fair balance of opportunities in the world's trading system.

Later this year, I will lead a ten-member delegation to China to meet with senior officials within that government. We will try to focus attention on the continuing cultural barriers that inhibit expanded U.S.-China trade.

The point is, Mr. Chairman, that the U.S. Chamber is actively involved, day-to-day, in promoting an improved climate for American business around the world. We cannot simply support an open trading system at home without recognizing that we have an obligation to pressure constantly for improved condition for our exporters and investors abroad. We were particularly pleased to note that in the House State Department authorization bill strong new language has been included to task U.S. ambassadors around the world to work toward improved market access. This new directive, if passed by Congress and implemented with aggressiveness, will help reinforce the activist posture already shared by thousands of American business executives.

Conclusion

Mr. Chairman, I would like to conclude my testimony by pointing out that the stakes involved in the clamor for protectionism are difficult to overstate. As I mentioned earlier, our trade interests cannot be separated from our broader domestic and foreign policy interests. When we fail in one area, the others are also at risk. World commerce, as much as anything, is the glue that holds mankind together. Trade with other nations necessarily forces all of us to recognize how important we are to each other, and how much we depend on each other. It is through mutual recognition and mutual dependence that all of us can strengthen the foundation upon which to build a better, freer and more prosperous world.

I have included with my statement attachments explaining in greater detail the Chamber's position on a number of significant international issues, and I ask permission that they be included in the record. I would be pleased to try to answer any questions the members of this committee may have.

###

Chamber of Commerce of the United States of America
Washington

Statement on the U.S. Trade Deficit and Industry Protectionism

The outsized U.S. merchandise trade deficits expected in 1984 and 1985 reflect the serious disadvantages faced in the current macroeconomic environment by U.S. businesses in competition with foreign rivals.

The major sources of the U.S. trade deficit are (1) the gap between the strong growth rate here and growth rates abroad; (2) reduced purchases from the U.S. by debtor developing countries; and (3) the strength of the dollar relative to foreign currencies. The deficit does not, however, indicate that U.S. industries are fundamentally weak or that they are being overtaken by unfair foreign competition.

Consequently, protectionist measures, such as an import surcharge, domestic content laws, and restrictive trade laws, are not a proper or effective means for reducing our trade deficit. On the contrary, import restrictions are apt to exacerbate the deficit in the future by further strengthening the dollar and frustrating the overseas recovery that is crucial to the revival of U.S. sales abroad. Particularly counterproductive would be import restraints that would further erode the already impaired ability of indebted developing countries to pay for U.S. exports. Nothing here should be construed as condoning imports to the United States priced below fair value or those benefitting from foreign government subsidy (as defined in applicable trade law), nor as opposition to United States corporations seeking redress under existing law and regulation against such imports.

Although protectionism is the wrong response to our trade deficit, the U.S. Chamber is concerned that, if sustained, the macroeconomic factors that have created the deficit will cause serious world market losses and the contraction of domestic industries that are fundamentally competitive. To prevent this, the U.S. should encourage policies overseas that invigorate foreign demand and support foreign currencies by creating conditions favorable to growth, adjustment, and expanding world trade. A key force for stimulating economic vitality overseas would be the dismantlement of foreign barriers to trade and investment while the U.S. works at the same time to keep its markets open.

November 1984

Chamber of Commerce of the United States of America
Washington

Statement on Bilateral Trade Agreements

The Chamber continues to advocate multilateral negotiations and agreements as the best means to reduce barriers to world commerce, and supports the principle of non-conditional most-favored-nation treatment as a general norm. Bilateral agreements, and any preferential arrangements among countries, should be avoided because they risk the erosion of the multilateral framework that best serves the free flow of trade and trade-related investment. However, exceptions may be justified if it can be demonstrated that bilateral agreements or arrangements are necessary to create momentum for multilateral negotiations for a more open trading system, or if multilateral action is highly improbable within a reasonable timeframe.

June, 1984

Chamber of Commerce of the United States of America

Washington

Statement on Managed Trade

The growing interest in and use of "managed trade" -- a term used to describe explicit or implicit deals between or among governments, with or without the participation of private parties, to limit import shares in a given market -- in general runs counter to the United States' interest in an expanding and open world economy. At the same time, managed trade may be a practical tool for affording to U.S. industries that have demonstrated injury due to fairly-traded imports the temporary import relief authorized by U.S. law and international agreements.

Therefore, the Chamber of Commerce of the United States believes that managed trade should be employed as a tool of import relief solely within the confines of the standards and procedures of the two major trade statutes offering relief from fairly-traded imports, Section 201 of the 1974 trade law (the so-called "escape clause") and Section 204 of the Agricultural Act of 1956.

The Chamber recognizes that efforts to manage trade outside the confines of these statutes nonetheless are apt to continue. If so, in all cases of managed trade for import relief from fair trade or for any other purpose, the process leading to managed trade should be transparent. The President should publish in the Federal Register an Executive Order announcing his intention to consider, negotiate, enter into, or accept an agreement or arrangement with a foreign government or exporter to restrain trade. Similarly, he should by the same means make notification if he has reason to believe that a foreign government or exporter is acting, or plans to act, to restrain its exports to the U.S. market. At the same time, the President should request comments on these actions.

At a later date, the President should publish in the Federal Register the results of any such negotiation or foreign action to restrain trade. At that time, the President should report on the anticipated costs and benefits of the results to the affected U.S. industries, including users of the restrained product, and to consumers. He should also report on the anticipated overall effect of these results on the U.S. economy.

In all cases of managed trade for import relief from fair trade, the link between such relief and action toward industry adjustment should be improved.

All managed trade for the purpose of import relief from fair trade should be limited in duration at the outset. Any renewal of such relief should be made subject anew to the same criteria and procedures identified for first-time import relief.

Chamber of Commerce of the United States of America

Washington

Statement on Proposed General Agreement on Tariffs and Trade (GATT) Round for 1986

The U.S. Chamber of Commerce's position regarding a proposed 1986 General Agreement on Tariffs and Trade (GATT) Round is as follows:

1. The Chamber supports new and dedicated multilateral efforts to reduce barriers and to restore and improve discipline and stability in the world trading system. The nature of the trading world has changed, and protectionist actions have increased sharply since the last multilateral trade negotiations in 1979. Import barriers and other trade-distorting practices have multiplied, often nullifying past agreements. New and better solutions, covering a wide range of possibilities, must now be sought.
2. Greater flexibility in the actual GATT procedures, techniques and negotiating style is needed, due to constantly changing worldwide economic conditions.
3. The convening of a representative GATT Preparatory Committee is overdue and its hard task of agreeing on an agenda and the means of pursuing its goals must begin. A disciplined and more stable international trading system will require this initial consensus among nations, developed and developing alike, on what must be sought and how.

The Chamber believes that the priorities for these new efforts are at least sevenfold: (1) to strengthen the disciplines of the international trading system, and to seek further reductions of non-tariff and tariff barriers (to do this, we must reappraise the successes or failures and reasons for such results of the Tokyo Round Codes and the GATT itself, and review issues such as Most Favored Nation Treatment, permissive customs unions and free trade areas, safeguards, dispute settlement, and government intervention in trade); (2) to examine GATT machinery and the role of its Secretariat in order to improve its performance; (3) to help GATT adapt to the emerging needs of services, investment and intellectual property rights issues; (4) to review the linkages between trade and monetary matters; (5) to assist developing countries assume a more active and responsible role within the world trading system; (6) to secure maximum public support in order to improve present trading rules and institutions and to provide directions for solutions to other new or yet to emerge problems; and, (7) to seek renewed Presidential negotiation authority from the U.S. Congress.

Assuming that these multilateral negotiations do not conclude for a number of years, it is critical that any trade problems that arise in the interim be resolved through bilateral, GATT Plus, or plurilateral mechanisms, and be consistent with the U.S. objectives of the multilateral round.

In light of this, the Chamber believes it would be premature for it to take positions on specific issues or comment on detailed solutions until more preparatory work is done. The Chamber will become involved in this preparatory effort.

Chamber of Commerce of the United States of America
Washington

Statement on U.S-Japan Trade Relations

The dramatic increase in the bilateral trade deficit with Japan from $19 billion to $37 billion in two short years, the continuing need for reduction of trade barriers, and highly volatile exchange rate movements are causing a crisis in the domestic political arena. Such events could result in the Congress taking ill-conceived actions that might appear to alleviate the trade balance problem, but which could actually result in exacerbating the situation.

It is vitally important that our policy makers in Congress and the Administration carefully define the trade problems to be solved. Both nations need to share leadership and responsibility for maintaining and expanding a global trading system which is truly open.

Given the critical nature of the situation, the Chamber reviewed pending legislation and Administration proposals, and made the following policy recommendations:

1. The Chamber opposes legislation that mandates the President to take retaliatory action against any country, since the Chief Executive must retain the flexibility he has under existing law which permits him to initiate specific actions based on his perspective of the national interest.

   We oppose such legislation for the following reasons: The potential of such a law not being in compliance with existing international obligations; the irrelevance of such broad retaliatory action based on response to an industry specific action; and the fact that such retaliatory action will not gain better access to Japanese markets. The Chamber continues to support current trade law which is designed to counter unfair trade practices that inhibit market access to U.S. exports.

2. The Administration should push the Japanese harder on market access through the traditional mechanisms of bilateral negotiations and agreements, and General Agreement on Tariffs and Trade (GATT) procedures, including Article XXIII, "Nullification or Impairment", on a case-by-case basis. The objective of the Administration should be to develop a more coherent trade policy with Japan in order to significantly increase efforts to gain access for U.S. investment, products, and services.

3. In the event that these traditional mechanisms do not accomplish access for U.S. investment, products, and services within a reasonable period of time, the U.S. should utilize its rights under domestic and international trade laws, and reconsider such unilateral actions as may be appropriate, and consider major changes in existing domestic and international arrangements governing trade.

Attachment

Statement on Access to Worldwide Telecommunications Markets

The U.S. Chamber supports an active program of U.S. government bilateral and multilateral negotiations to remove foreign barriers to U.S. exports. The critical role played by telecommunications in international trade of high technology products and services gives a special urgency to efforts to address specific barriers to international trade in telecommunications products and value added telecommunications services. Therefore, the U.S. Chamber welcomes legislative initiatives to encourage the Administration to negotiate greater access for U.S. firms to worldwide telecommunications markets, provided that such legislation conforms to the following principles:

1. The aim of U.S. initiated negotiations should be to achieve open trade in telecommunications products and services.

2. Legislation should provide a mandate to the Administration to negotiate the reduction or elimination of barriers to telecommunications trade and should include the authority to negotiate the elimination of any remaining U.S. barriers.

3. Progress towards greater access should be determined by monitoring the results of existing and future trade agreements to assure that all barriers are removed.

4. The U.S. government should take flexible and credible action to enforce existing agreements and to restore competitive opportunities if negotiations fail to produce significant progress towards a more open market.

5. Any bilateral agreements entered into by the U.S. government should be supportive of future multilateral negotiations and the international trade and investment system.

6. Legislation to the extent possible should encourage the use of existing U.S. government trade authority.

Major International Trade Actions:
Reagan Administration
1/1/81-8/23/84

FREE TRADE

1. 4/14/81
President approves ITC recommendation to increase peanut quota by 300,000 pounds during the period of August 1980-July 31, 1981

2. 6/30/81
President removes OMA's on shoes from Korea and Taiwan.

3. 7/8/81
Administration issues statement on "U.S. Trade Policy."

4. 3/8/82
Department of Commerce finds no subsidies on Canadian lumber.

5. 4/9/82
President rejects quotas on casein imports.

6. 10/8/82
President signs Export Trading Company Bill.

7. 4/26/83
President rejects Houdaille petition, (Machine Tools).

8. 8/5/83
President signs Caribbean Basin Initiative

9. 9/15/83
Administration increases sugar quota by 150,000 short tons for FY'84.

10. 11/30/83
Administration signs law increasing share of U.S. funding to the IMF.

PROTECTIONIST

1. 4/1/81
Japanese initiated Voluntary Restrain Agreement on automobiles with U.S.

2. 9/11/81
Administration levied a 1 cent a pound import fee on imported raw sugar.

3. 12/22/81
Renewal of Multifiber Agreement. U.S. pushed for restrictive section. Restrictive textile bilaterals were agreed to through 1984.

4. 12/22/81
Farm Act of 1981 approved by Administration (wheat, corn, rice, sugar, peanuts, dairy, meat).

5. 10/20/82
Administration announces 3-year, $1.5 billion agricultural export credit program that will benefit from subsidized interest rates. President approves ITC recommendation to increase peanut quota by 300,000 pounds during the period of August 1980-July 31,1981.

6. 10/4/82
President promised import regime on textiles which would "relate" imports to growth in domestic consuption.

7. 10/21/82
U.S.-E.C. Steel Agreements to restrain imports of EC steel into the U.S.

11. 8/6/84
Administration rejects ITC recommendation to impose quotas (425,000 tons) or raise tariffs (by .05 cents per pound) on imported copper because restrictions were "not in the overall national economic interest."

12. 8/18/84
Administration rejects ITC recommendation to impose quotas on steel imports and a tarriff quota on semi-finished steel.

Compiled by:
Consumers for World Trade/Washington, D.C.

8. 1/15/83
Administration imposed a unilateral ceiling (700 million level reached in 1982) on imports of Chinese textiles.

9. 1/18/83
(Egypt)
Administration subsidizes wheat flour sales to Egypt, Morocco and Iraq in retaliation to subsidized EC sales of wheat and flour.

10. 4/1/83
President approves 45% increased duties on imported motorcycles.

11. 5/10/83
President reduces quotas on sugar from Nicaragua by 90%. Action taken in retaliation for Nicaragua's support of guerilla activities in Central America.

12. 7/5/83
President imposes tariffs and quotas on a wide range of specialty steel products for 4 years.

13 12/16/83
President agreed to tighten restrictions on textile imports. The restrictions addressed themselves to "low-waged third market nations.

14. 8/3/84
Administration announces new "country-of-origin" provisions on textile imports.

15. 8/18/84
Administration calls for negotiated cutback of steel imports to 18.5% of the American market.

Attachment

Statement on Proposed General Agreement on Tariffs and Trade (GATT) Round for 1986

The U.S. Chamber of Commerce's position regarding a proposed 1986 General Agreement on Tariffs and Trade (GATT) Round is as follows:

1. The Chamber supports new and dedicated multilateral efforts to reduce barriers and to restore and improve discipline and stability in the world trading system. The nature of the trading world has changed, and protectionist actions have increased sharply since the last multilateral trade negotiations in 1979. Import barriers and other trade-distorting practices have multiplied, often nullifying past agreements. New and better solutions, covering a wide range of possibilities, must now be sought.

2. Greater flexibility in the actual GATT procedures, techniques and negotiating style is needed, due to constantly changing worldwide economic conditions.

3. The convening of a representative GATT Preparatory Committee is overdue and its hard task of agreeing on an agenda and the means of pursuing its goals must begin. A disciplined and more stable international trading system will require this initial consensus among nations, developed and developing alike, on what must be sought and how.

The Chamber believes that the priorities for these new efforts are at least sevenfold: (1) to strengthen the disciplines of the international trading system, and to seek further reductions of non-tariff and tariff barriers (to do this, we must reappraise the successes or failures and reasons for such results of the Tokyo Round Codes and the GATT itself, and review issues such as Most Favored Nation Treatment, permissive customs unions and free trade areas, safeguards, dispute settlement, and government intervention in trade); (2) to examine GATT machinery and the role of its Secretariat in order to improve its performance; (3) to help GATT adapt to the emerging needs of services, investment and intellectual property rights issues; (4) to review the linkages between trade and monetary matters; (5) to assist developing countries assume a more active and responsible role within the world trading system; (6) to secure maximum public support in order to improve present trading rules and institutions and to provide directions for solutions to other new or yet to emerge problems; and, (7) to seek renewed Presidential negotiation authority from the U.S. Congress.

Assuming that these multilateral negotiations do not conclude for a number of years, it is critical that any trade problems that arise in the interim be resolved through bilateral, GATT Plus, or plurilateral mechanisms, and be consistent with the U.S. objectives of the multilateral round.

In light of this, the Chamber believes it would be premature for it to take positions on specific issues or comment on detailed solutions until more preparatory work is done. The Chamber will become involved in this preparatory effort.

Attachment

Statement on

Exchange Rates and U.S. Competitiveness

The recent appreciation of the U.S. dollar compared to other major currencies in foreign exchange markets -- over 50% since 1981 on a trade weighted basis -- is a major cause of the increase in the U.S. merchandise trade deficit during that period. Other factors, such as growth rate differentials, third world debt crises, and unfair trade practices are also important. But taken together, these factors account for less than half of the increase in the U.S. merchandise trade deficit. The strong U.S. dollar, having contributed much to our record merchandise trade deficit, is placing exporters and import-sensitive industries at a severe disadvantage in world markets. Perhaps even more significantly, the strong dollar is increasingly responsible for U.S. business decisions to locate investment and jobs offshore and otherwise distort investment decisions, which further undermine the U.S. industrial base and competitive position.

The principal explanation for the dollar's rapid appreciation lies in the U.S. fiscal policy since 1981. During that period, U.S. budget deficits have risen from $79 billion to over $225 billion, and have been a major factor in keeping U.S. interest rates higher than they would have been in a period of greater fiscal restraint. These budget deficits have exacerbated an ongoing shift in net international capital flows into the United States. This shift in capital flows, reflecting the substantial worldwide demand for dollar-denominated assets, has kept the dollar's exchange value far higher than would normally be expected during a period of high U.S. merchandise trade deficits.

The single most important action the U.S. government can take to reduce the dollar's exchange value and the trade deficit is to sustain efforts to reduce federal government spending. In this manner, reduced budget deficits can serve to bring interest rates down, and bring the dollar's exchange value down to a level that will lead to smaller trade deficits.

At the same time, the United States should continue to cooperate with the other "Group of Five" nations (France, Germany, Japan, United Kingdom), who jointly announced on September 22, 1985, that they would "pursue, individually in our own countries and cooperatively together, policies conducive to sustained growth and higher employment." At that time, the "Group of Five" also pledged to continue to oppose protectionist measures, including import surcharges, quotas, domestic content laws and other restrictive trade measures, which would only serve to reduce total world trade, and lead to slower economic growth, lower incomes and higher unemployment.

Attachment

Recommended Revision in Policy on International Finance - Monetary Policy

Present Policy	Proposed Revision
Monetary Policy. International monetary policy should be directed toward providing the framework for the largest possible expansion of world trade consistent with reasonable stability and flexibility in international monetary relations. Since international monetary values are closely related to the value of the dollar, the United States must assure the strength of the dollar without resorting to exchange restrictions and other controls.	**Monetary Policy.** International monetary policy should be directed toward providing the framework for the largest possible expansion of world trade consistent with reasonable stability and flexibility in international monetary relations. Since international monetary values and the U.S. external position are closely related to the value of the dollar, the United States must assure the dollar's exchange value in a manner consistent with movement toward balance in the U.S. external position and without resorting to exchange restrictions and other controls.

U.S. Council for an Open World Economy
INCORPORATED

7216 Stafford Road, Alexandria, Virginia 22307
(703) 765-2472

Statement submitted by David J. Steinberg, President, U.S. Council for an Open World Economy, to the U.S. Senate Committee on Finance in oversight hearings on U.S. trade policy. November 21, 1985

(The U.S. Council for an Open World Economy is a private, nonprofit organization engaged in research and public education on the merits and problems of developing an open international economic system in the overall national interest. The Council does not act on behalf of any "special interest".)

The United States has no strategy (it never did) to program totally fair trade with other countries -- total in its coverage of all policies and practices affecting international commerce and its concern with total fairness in those policies and practices. Nor is there a strategy (there never has been) to program totally open, totally free international trade -- the removal of all artificial barriers and distortions in accordance with a realistic timetable. Charter membership in the General Agreement on Tariffs and Trade, and participation in the many GATT rounds of trade negotiation, do not add up to the definitive strategies I have in mind. Never in place with respect to goods alone, they are needed today both for goods and services, and for international investment as well. The time has come, it is already many years late, to establish clear, convincing strategies of this scope on the nation's highest-priority agenda in domestic and foreign policy.

Much rhetoric has advanced the proposition that we need "fair trade" as well as open trade. Some have argued for "fair trade" but do not propose free or substantially freer trade. Conspicuously absent are policy proposals likely to achieve the fairness so fervently sought. I am here reiterating a trade-policy proposition I have articulated in many statements to Congressional committees in recent years.

We must earnestly and explicitly seek both *free* trade and *fair* trade as integral, inseparable, indispensable dimensions of a coherent trade policy. Totally fair trade is not achievable except in conjunction with a commitment to totally free trade, and vice versa. In addition to the coventional definitions of unfairness (injurious dumping, harmful subsidies, etc.), disparities in tariff and nontariff barriers affecting particular goods and services are themselves instances of unfairness in today's world economy, calling for efforts to program their removal. Moreover, there will not be sufficient incentive to seek *total* fairness over the entire range of trade policies and practices (no exceptions) except under the extraordinary spur of a commitment to totally free trade. Conversely, there is no practical possibility of programming totally free trade (the negotiated removal of all artificial barriers to international commerce in accordance with a realistic timetable) without contractual assurance that the trade between the countries that enter into a free-trade compact will pari passu be fair. Free-trade programming of maximum, optimum reciprocity will ensure the most constructive, most trade-expansive reciprocity. And one of the most productive adjuncts -- in fact, one of the priority prerequisites -- of a deliberate free-trade initiative will be (at long last) an incisive effort to find real solutions to serious problems of U.S. competitiveness in a rapidly changing world -- avoiding trade restriction except as last-resort, emergency components of coherent adjustment strategies addressing the real problems of these sectors of our economy.

Some progress can be made in making international trade more fair through a multilateral negotiation much less ambitious than a definitive free-trade initiative. More progress toward freer trade is attainable through the mode of multilateral negotiation to which we have become accustomed over the last half-century and which characterizes the planning now under way for the round of the 1980's. But many areas of unfairness will escape reform, and new forms and degrees of unfairness will enter the vacuum of neglect. Unlike nature, protectionism does not abhor a vacuum: protectionism adores a vacuum. Moreover, any hope of significant progress in reducing and removing barriers to trade in services without a far-reaching (ideally free-trade) commitment on barriers to trade in goods is a flight of fancy. Nor can significant if any progress be made on the stickiest areas of trade restriction (agricultural products, textiles, steel, to mention just a few at random) except within the framework of a dramatic, comprehensive negotiation embracing all products, policies and practices (no exceptions) under an explicitly free-trade arrangement establishing a timetable that could (and should) be different for some products, etc. from that for others.

How to get from where we are in trade-policy planning to where we ought to be. The device suitable to this purpose would be a Presidential invitation -- formulated after appropriate consultation with Congress -- to the economically advanced countries to join us in negotiating a free-trade area (with a suitable code of fair competition) in accordance with the rules of the General Agreement on Tariffs and Trade. (Special arrangements would have to be made for underdeveloped countries prepared to make appropriate commitments within their range of capability.) The United States would be prepared to enter into such a compact with as many countries as cared to participate, even if only one other country responded positively. The door would be left open for others to join, but non-members would be denied the customs treatment enjoyed by members until membership is attained. All would join sooner or later, for none could afford to be left facing the regular trade restrictions of member countries while member countries remove barriers affecting one another. This is the route to take if a truly free-trade arrangement is to be forged between the United States and Canada, not the route currently under consideration. The same was true of Israel, and I so argued in presentations to Congressional committees.

An astutely orchestrated free-trade initiative of the type only briefly sketched in this statement would provide a trade-policy premise of inestimable value and potential to the decision-making both of U.S. producers and government. A free-trade premise factored into planning in the private sector would induce more-soundly based decisions in meeting international competition and more effective efforts in export promotion with respect to foreign markets that are party to the free-trade agreement. A free-trade premise factored into the decisions of government would induce more-soundly based judgments in helping needy and deserving sectors of our economy, and in measures to facilitate and stimulate the economic redevelopment (including industrial adjustment) that merits priority attention in domestic policy.

Fiscal, monetary and other areas of public policy would have to be synchronized with this free-and-fair-trade strategy whose time has come. Fairness in exchange rates is a priority issue.

U.S. trade policy, including explicitly the attention given the question of unfair trade practices (a major focus of these hearings), is a long way from the approach that is urgently needed and without which the slippage endemic on today's slippery slope of trade liberalization could offset much of the progress likely to be made in negotiating freer trade with the devices now employed. The Executive Branch is inadequately structured for forging and sustaining the strategy that is needed both in foreign-economic and domestic-economic terms -- a subject I have discussed elsewhere and shall address again in appropriate hearings.

The Administration, responding largely to threatened protectionism from Congress, is "getting tough" in trade policy, especially in regard to "unfair" practices by foreign governments and foreign exporters. But it is avoiding and evading the tough decisions that need to be made in trade policy, fiscal and monetary policies and "industrial policy" if real, durable solutions are to be found to the problems we encounter in increasingly intensive foreign competition. Responding to questions put in the Finance Committee's press release announcing these hearings: Yes, we can move effectively and sensibly against unfairness in international trade practices; there is a way, but no evidence of the necessary will and wisdom. Yes, we can compete with "fair" trade, but American business needs the certainty of more-astute, more-prudent, government policies in trade and related fields to factor into its decisions, and government is unprepared for the dramatic new initiatives that are long overdue in this regard.

The kind of multilateral trade negotiation now being planned would divert government energies and those in the public sector from the domestic-economic and foreign-economic reforms and initiatives needed at this critical time for the American economy and the international trading system. The trade-negotiation initiative for the 1980's must seek all that the nation needs. Critics of so ambitious an undertaking may reply that half-a-loaf is better than none at all and could be productive, notwithstanding its limitations. But why settle for half-a-loaf for the opening salvo for the one and only negotiating round of the 1980's? The next round won't come until the 1990's. We cannot afford the luxury of postponing for at least 10 years the initiative that merits our most earnest efforts right now.

What I have proposed requires a brand of Presidential leadership that is not yet evident, and Congressional profiles of courage still to be found. The so-called "free traders" (almost without exception) in the country at large are themselves wallowing in jaded notions of "freer trade" and "liberal trade", far back from the new frontier in trade policy where I am waiting for them to show up. All in all, America is unprepared in this policy area so vital to its economic well-being, political stability, indeed its national security.

NATIONAL RETAIL MERCHANTS ASSOCIATION

This statement presents the views of the National Retail Merchants Association ("NRMA") on the appropriate direction of United States trade policy in general and as applied to "unfair" and "fair" trade practices. We appreciate the opportunity to present these views and would be pleased to explain or elaborate on the comments made in this statement.

By way of background, NRMA is a national, nonprofit trade association composed of over 3700 members who operate more than 40,000 department, chain and specialty stores in the general merchandise retail industry. Our members have an aggregate annual sales volume in excess of $125 billion and employ over 3 million workers.

NRMA and our colleagues in the retail industry have been consistent advocates of the removal of barriers to international trade. We believe that minimizing such artificial restraints on the worldwide marketplace has obvious, significant benefits for American consumers and American exporting industries (and the workers in those industries), as well as for our own businesses. Further, we believe that competition from worldwide markets will, even in the relatively short term, strengthen those American industries which compete against imported products. Even in the rare case where an American industry must undergo substantial adaptation due to such competition, we believe that such industry will often strengthen itself in response. The overall result of an effective trade policy is a much healthier American economy.

Notwithstanding the benefits of trade as described above, we recognize that unfettered trade cannot always be countenanced. Specifically, trade which is "unfair" should not be permitted to injure U.S. industry. By "unfair trade," NRMA is not referring to trade fostered by comparative advantage, including lower wage rates, but, rather, to a variety of trade practices which should not be permitted to injure U.S. industry. In this regard, we believe that the laws of this country effectively provide remedies against "unfair" trade practices.

With respect to imports, several legal remedies are available:

-- The antidumping law,[1] which is an international price discrimination law, imposes a duty on imports (1) if such imports are sold in the United States at less than foreign market value and (2) if such sales cause or threaten material injury to a U.S. industry. The duty is equal to the amount by which the foreign market value exceeds the United States price.

---

[1] Tariff Act of 1930, as amended by the Trade Agreements Act of 1979, 19 U.S.C. §§ 1673-1677g.

-- Under the countervailing duty law,[2] if a foreign government or private entity provides a subsidy upon the manufacture or exportation of merchandise and (in certain cases) if the International Trade Commission determines that imports of such merchandise have caused or threaten material injury to a U.S. industry, a duty equal to the amount of the subsidy is imposed on the imported merchandise.

-- The broad language of Section 337 of the Tariff Act of 1930 ("Section 337")[3] indicates that the Section is directed against a wide variety of unfair practices in import trade. Traditionally, Section 337 has been applied to imported goods that infringe U.S. patents. Recently, however, the statute has also been used to counter violations of copyright and trademark law in the course of import trade.

In addition, Section 301 of the Trade Act of 1974 ("Section 301")[4] accords the United States Trade Representative and the President broad powers to respond to unjustifiable, unreasonable, or discriminatory trade practices by foreign countries or instrumentalities which adversely affect United States commerce -- either in terms of impeding U.S. exports or in improperly stimulating imports into the U.S.

---

[2] Tariff Act of 1930, as amended by the Trade Agreements Act of 1979, 19 U.S.C. §§ 1671-1671f; 19 U.S.C. § 1303.

[3] As amended 19 U.S.C. § 1377.

[4] As amended, 19 U.S.C. § 2411.

NRMA believes that the above-described laws effectively provide what constitutes "unfair" trade practice. The antidumping and countervailing duty laws are consistent with standards widely agreed to in the international community. Section 301 has been invoked to enforce various Codes under the General Agreement on Tariffs and Trade ("GATT"). Moreover, Section 337 embodies general concepts of unfairness which are common in U.S. law (*e.g.*, Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45). Thus, we believe that United States law provides effective remedies against unfair trade practices.

As to fair trade, the law also provides a remedy. Section 201 of the Trade Act of 1974 ("Section 201")[5] accords seriously injured U.S. firms temporary relief to adjust to freer conditions of international competition. More specifically, under Section 201, upon determination that an article is being imported into the United States in such increased quantities so as to substantially cause serious injury or threat thereof with respect to a like or directly competitive domestic article, the International Trade Commission recommends to the President the type and amount of relief necessary to remedy the injury. We believe that the statute identifies appropriate factors for the President to consider in determining whether to grant relief and that it is essential that he continue to have discretion in this area in order that the national interest is in fact furthered.

---

[5] 19 U.S.C. §§ 2251-2253.

Finally, the current trend of protectionism -- as illustrated by proposals of enactment by the U.S. of new, unilateral laws, and by negotiations of ad-hoc "voluntary" arrangements with foreign countries -- must be resisted. The experience of the retail industry in living with the problems of expanding protectionism in the textiles and apparel sectors under the Multi-Fiber Arrangement ("MFA") is a telling example of how departures from the multilateral, open-market approach espoused by GATT and existing U.S. trade law, are a serious mistake. In our assessment of the renewal of the MFA (copy of document attached), we concluded that the extraordinary protection provided to the U.S. textile and apparel industries via the 30-year program of managed trade erected by the MFA has served the interest of no one -- neither retailers, their customers, nor the textile industry as a whole has benefited. On a more general level, a national battle that promotes protectionism victimizes the consumer in the end, who becomes deprived of the lower prices and variety provided by imported goods as well as of the additional deflationary effect caused by the mere presence of imports in the marketplace. Furthermore, construction of trade barriers may invite retaliatory measures from foreign countries and thus exacerbate the United States' position in the international market.

○